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ENTERING IN THE SOUTH AFRICAN MUSIC STREAMING MARKET – INTERNATIONALIZATION STRATEGY OF NMUSIC

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#1472

A Project carried out on the Field Lab in Entrepreneurial Innovative Ventures, under the supervision of:

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Executive Summary

To enter on a foreign market, a company needs to understand the market and industry drivers of the chosen country, as they will impact the potential profitability, assess if its current structure with strengths and weaknesses allows the movement, and which are the customers' needs that the portfolio of products and services will have to answer. Briefly, it has to build an in-depth strategy before starting the international venture. The aim of this work project is to present a detailed internationalization strategy for the Portuguese streaming music start-up nMusic to enter in South Africa on a partnership with the TV channel network, TRACE. This choice as a partner on the entry mode is based on a suggestion from nMusic CEO, Celestino Alves. This indication follows a series of contacts between nMusic and TRACE executives to create a streaming service in South Africa under TRACE brand with nMusic technological infrastructure and music agreements. Our Work Project will be delivered to nMusic executives to assist them on the strategic decision of entering in South Africa.

To accomplish the general goal of this work project, its structure is as follows: a research methodology was built around key research tools – PESTEL Analysis, Industry Mapping, Competitive Assessment and the 5 Forces of Porter - to evaluate and propose recommendations on the external environment, considering the South African market and the industry of digital music. On the internal analysis, insights are presented about nMusic resources that will help to shape and maintain a Competitive Advantage in South Africa. To build a profitable venture, a Revenues and Costs structure is proposed in alignment with market competitors, relevant cost drivers and an online survey conducted. The Products and Services portfolio of nMusic proposal has in consideration market studies and also the survey results. The collaborative arrangement that will turn effective this partnership is a technology licensing agreement with nMusic music platform being used under TRACE brand to reach end-consumers. As all this factors exist on a dynamic and challenging environment, a SWOT/TOWS analysis and a Risk Assessment are also part of this work to provide warnings, stress recommendations and improve the partnership strengths because it will increase the likelihood of success of the partnership business model between nMusic and TRACE.

Keywords: Digital Music, Streaming, Record Labels, Internationalization Strategy, South Africa, nMusic, TRACE, Technology Licensing Agreement.

Research Methodology Approach

The entire content of this work project is built around one Main Research Question: "*What is the most suitable internationalization strategy for nMusic to enter in the South African digital music market?*" In order to provide the best add-valuable answer to it, our approach will be "deductive" (Harvey, L., 2012), asserting general conclusions from a given set of premises/events and "interpretive" (Burrell and Morgan, 1979), with specific interpretation being made over both secondary (market research studies) and primary market (online survey) research. The Main Research Question will be decomposed into Sub-Research Questions to analyse specific topics and challenges. These subsequent questions have a narrow scope and, as a consequence, enable more direct and meaningful answers to present a final solution for the Main Research Question. These responses will be provided through several chosen Research Methods where information is filtered and disposed on a comprehensive manner. For each sub-research question we will have a specific research method, for example, to understand and discuss the current stage and main trends shaping the digital music market, a Literature Review will be performed; a PESTEL analysis will be used to make a general overview about the present and medium term future of South Africa; to refer to nMusic core resources and capabilities that impact their competitive profile a VRIO Framework analysis will be conducted; to assess relevant stakeholders to nMusic in South Africa an Industry Mapping will be the research method; to list and understand the ways external and internal business factors shape and influence nMusic performance will require the use of a TOWS/SWOT matrix; to evaluate the level of competition that the company faces a Porter 5 Forces analysis will be used; and finally, to ensure that i) a strong value proposition is made, ii) P&S portfolio and pricing matches customers' needs and expectations, iii) segmentation, target and positioning are aligned with the partnership goals and objectives, market studies and an online market survey will be our research tool. Figure 1 presents an *Issue Research Tree* where all the research methodology is graphically structured.

Main Research Question

What is the most suitable internationalization strategy of nMusic to enter in the South African music streaming market?

Sub-Research Questions	Research Method
How music industry evolved and what is the current phase and trends shaping the music and digital music markets?	Literature Review
What are the main characteristics and challenges on the present and medium term future of South Africa?	PESTEL Analysis
What are the functionalities, features and service conditions on digital music that South African consumers value more?	Secondary (Market Studies) and Primary (Online Survey) Market Research
Which are the relevant stakeholders for nMusic service in South Africa?	Industry Mapping
What level of competition will nMusic service face in South Africa?	5 Forces of Porter
Which are nMusic main resources and capabilities that influence their competitive profile?	VRIO Framework
Which are the external and internal factors that will impact nMusic market position?	SWOT/TOWS Analysis

Figure 1 – Issue Research Tree

Literature Review

In order to provide the adequate research ground on historical evolution of the industry and market outlook a literature review was analysed. The modern music industry always relied deeply on the technological development, since its *product* to be distributed needs a mean to reach the audience. Back in the 1920's, artists realised that mass distribution was a good way to attract more fans – and revenues – to their songs, being an excellent advertising instrument (Blanchette, K., 2004). From the 1950s until the 1980s, the development of tape recordings happened due to the conception of the 12-inch long playing (LP) vinyl that enabled the music industry to soar. The new technology was responsible for lowering production costs and the minimum efficient scale of production, facilitating the entrance of new smaller and independent companies in the industry. To consumers, it represented a progress on their relationship with music, since with less expensive investments the middle class could acquire a good tape recorder to listen LP. But on the late 1970s the industry started to slow down its growth. It was only in 1983 with the Compact Disc (CD) introduction that a new phase of growth began and the sector kept a good track until the mass penetration of Internet and new ways of listening music were brought up (Blanchette, K., 2004). The late 90s technological developments brought radical changes to the industry with the introduction of the MP3 format. On the early 2000s, MP3 rapid popularity gave origin to peer-to-peer networks and online music communities, such as Napster and MySpace (Collard, L. 2008), having the latter reached a peak of 100 million users,[1] and with the chance of download any song they wanted. This led to several lawsuits[2] due to of digital piracy and copyright infringement. Napster was turned off in July 2001. Despite this, when it was shut down, the online music revolution was already in progress (*on Appendix 1 the shift from physical recorded music to digital forms is graphically presented*). As illegal downloads soared, physical sales started to decrease.[3] Consumers started to perceive music as free, available everywhere, whether for sharing or for download, becoming a day-to-day activity, still a major trend today. The transportable digital audio players, like Apple's iPod introduced in 2001, removed the need to carry CDs or tapes and transferred the concept of music listened on a CD (object) by a total music experience in quotidian (feeling). Digital music growth goes intimately related with illegal means of getting music online. Considering the digital music piracy, that in South Africa it accounts for about EUR 36.3 million (2013 numbers) in the music industry revenues,[4] our analysis must go deeper and understand the causes and some effects of it. Collard emphasizes three causes of illegal downloads, i) like the financial issue, it is 'free ride'; ii) download's proximity and immediacy since songs appear online before the official release day; iii) and the fact that they provide a sample of the CD before the user decides to go physically and purchase it, enabling more complete information. This so-called Internet revolution had also impact on record labels, key members on the industry mapping, like the major big 4 - EMI, Sony, Universal and Warner Music Gallo-Africa - that were afraid of a dramatic change on the traditional music distribution chain where artists depend on record labels to record song and have them shared. The arrival of new distribution channels could eventually harm the big brands since those online communities were a strange agent in the industry that in few time got millions of users, intimidating their oligopoly (Collard, L. 2008) and increasing the threat of new entrants

[1] Mashable. *MySpace Hits 100 Million Accounts*, 09th August 2006. http://mashable.com/2006/08/09/myspace-hits-100-million-accounts/ (last access on 2014/10/28)
[2] BBC, *Metallica fans kicked off mp3 site*, 11th May 2000. http://news.bbc.co.uk/2/hi/entertainment/744664.stm (last access on 2014/10/28)
[3] Collard presents numbers saying that in US music retail sales plunged to $10.6 billion in 2003 from $13 billion four years earlier, in 1999.
[4] Data of the Southern African Music Rights Organisation (SAMRO)

(Porter, M. 2008) on the music market. The industry showed adaptation capacity to the download wave – signaling the introductory stage of digital music - and in 2003, Apple Inc. launched its online store, iTunes, to provide legal and licensed downloads to fans, having more affordable prices than the CD ones. Since then, iTunes has been a huge success,[5] helping the industry to grow reshaping it in a way that it is still dominant today: the digital download model, responsible for 67% of digital music revenues, is fostering the digital growth and momentum on several emerging markets, like South Africa (Digital Music Report 2014, hereafter DMR). According to IFPI,[6] in 2013 digital music accounted for 39% of total industry global revenues, representing a growth year-to-year of 4.3% to a value of US$ 5.9 billion. It is unquestionable that today's music industry landscape is shaped by the digital. On recent years, beyond download-based model, several services appeared with subscription-based models (sometimes also ad-supported, as Youtube) using a streaming technique, where a multimedia file can be played back without being completely downloaded first - *access* is prioritized to the *possess* of the file. We may say that introduction of streaming bring back the industry to a new introductory phase, considering its life cycle, since it is a new arrangement on the way music is distributed to consumers. Not merely a temporary trend, after 2009/2010 these streaming services established with long-term goals and projects. Companies like nMusic, Spotify or Deezer belong to this new digital segment, which accounts for almost 30% of digital music revenue (DMR 2014). A streaming service to thrive on this atmosphere has to present customized services, sharing communities, ability to download, recommendations based on the personal historic or video-clips. All this is happening on a challenging environment where digital music piracy is a key variable; ad revenues prove to be an insufficient way of monetising a business; more sophisticated consumers with wider choices; a fast expansion on emerging markets of digital music. The value proposition of a company as nMusic needs to embody these drivers and challenges because they will impact which features to display, if focused on access and experience or allowing more downloads, and how to collect revenues, since consumers on emerging markets, such as South Africa, are only now discovering the digital world and not used to loyalty schemes or long-term subscription packages.

[5] According to *Mashable* website, iTunes store's consumer base raised from 861 000 in 2003 to 5 million users in 2004, and as whole until 2006 users have purchased more than 1 billion songs on the platform.
[6] IFPI - International Federation of the Phonographic Industry is an organization that seeks to defend music interests. Founded in 1993, its world headquarters are located in London, United Kingdom.

Environmental Context Analysis

Understanding the market where nMusic will operate – South Africa – and its industry – Digital Music – is fundamental to assure a successful entry mode and a sustainable and profitable venture.

- *Market Overview*

With a population of 54 million, South Africa is the largest and most developed African economy. It is an emerging middle income economy, with abundant natural resources - diamonds, gold, platinum, other metals and coal - owner of a developed legal and financial system (its stock exchange occupies the 16th position worldwide), a reasonable network infrastructure and a system of communication and transport able to provide an efficient distribution of goods and services. The South African economy is based on services and administration, which contributes 70% to GDP and accounts for about 65% of the overall employment. Following, it is the industrial and mining sector, representing 27.6% of GDP (26% of employment).[7] After several years with growth rates above 5% on the beginning of the 2000s, its performance in 2008/09 suffered a significant slowdown, with the rate of GDP growth to be fixed at 3.6%[8] as a result of the international financial crisis. In 2010, the recovery of the international economy and the economic stimulus measures taken by the Government boosted the GDP growth to 3.1%. Over the last years, the GDP continued to grow but the unemployment rate, one of the world's highest, is still a laggard to sustainable growth[9] (*For more detailed macro-economic data see Appendix 2).* According to estimates by the Economist Intelligence Unit (EIU), the pace of economic growth will rise in 2014 and upcoming years driven by the set of fiscal impulses that strengthen private consumption and investment, higher wages and a weak currency, which favours the export sector. The country still faces some significant challenges, especially lack of qualifications, creating a unite community able to overcome ethnical segregation attitudes that still exist 20 years after Apartheid end, strong inequalities, crime and the fight against HIV. As major trends, we can identify significant economic growth over the last two decades, which improved disposable incomes and higher spending across all categories, appearing an

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[7] Data form the International Monetary Fund (IMF).
[8] *Economic Growth Statistics Report*, Statistics South Africa.
[9] Since 1997, the unemployment rate measured as a percentage of labour force has been always above 20% *(see graphical representation on Appendix 3*) and according with the South African official bureau of Statistics in 2014 it reached a peak of 25.5% in September 2014, the highest rate since 2008.

expanding middle class consumer base. There is a fast urbanization, causing a concentration of wealth and job creation in large cities (Johannesburg, Cape Town and Pretoria) and a rise on the use of cars and air travel. Despite all this, there is widening income gap between rich and poor (with luxury goods increasing tremendously). On consumer needs, we can identify a growing consumer sophistication and demand for convenience, boosting demand for products such as packaged foods, personal care items and private label goods. *On the appendix 4, a PESTEL Analysis is presented to draw a complete picture of the country.*

- *Industry Overview*

Regarding South African Media and Entertainment market, in 2014 it is valued on EUR [10] 9.6 billion with Internet accounting for 25% (EUR2.4 billion), while TV represents 24% (EUR2.3 billion) and music 1,5% (EUR153.4 million).[11] nMusic and TRACE partnership will face a market with a rising middle class (in number and income) that is making Internet the largest media and entertainment segment. Within it, mobile Internet access is leading due to the increasing number of subscribers – from 15 million South Africans in 2013 to 35.2 million in 2018 - as forecast by the consultancy firm PricewaterhouseCoopers (hereafter PwC). [12] According to PwC, there are two factors justifying this: affordable prices of smartphones and cheaper data plans. Based on the *South African Social Media 2014 Report*, the smartphone is by now the device through which the majority of South Africans access the Internet. As of March 2014, there were 19.9 million smartphones connections and the report estimates that, by the end of the decade, there will be about 50 million connections. Internet advertising is on a high growth phase, with revenues climbing from EUR116.8 million in 2013 to EUR321.4 million in 2018. In 2018, mobile Internet advertising will represent almost one third of the revenues with EUR87.6 million (in 2013, it accounted 18% of the total).[13] The South African digital technology market is on a booming phase and it is unquestionable its market potential for companies that offer content through apps and

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[10] According to XE Currency Converter (28th November of 2014) 1 EURO was equal to 13,69 South African Rands. In this work project, all the monetary values will be presented in the EURO currency.

[11] A figure with current data and future projections of Media and Entertainment market value made by PwC is presented on the Appendix 5.

[12] In the next 5 years, Internet access will produce more consumer spend than any other media service. PwC market forecasts indicate that it will grow from EUR2.4 billion in 2014 to EUR5.2 billion in 2018 (more than double). Mobile phones are dominating the SA Internet access market with revenues totalling 1.5EUR billion in 2013, far more than the ones coming from fixed broadband devices on that year, EUR 284.9 million.

[13] *Entertainment and Media Outlook: 2014 – 2018, South Africa, Nigeria and Kenya*, PwC

browser services, as nMusic and TRACE do. As stated on the DMR 2014, a growing mobile Internet segment enables more consumer spending on digital music services. Considering 2014 total revenues, music market decreased by 3,3% [14] due to the significant drop on physical sales (-15,3% compared to the year before) and not totally offset by the increase on the digital segment (+37,5%), led by legal downloads and streaming services. Digital in South Africa is on the head of an industry transformation and it is the segment that is keeping the music market alive and with chances of a revival (*Appendix 6 presents a figure with comparison between physical and digital unit sales on the 2009 – 2018 timeframe*). On the figure 2, the South African music market is presented in revenues allocated by segments through a reasonable timeframe (2013 – 2018 years) with the correspondent CAGR[15].

							FORECASTS				
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	CAGR (2013 - 2018)
Physical	116.3	106.6	94.2	85.0	71.1	57.3	47.7	40.0	33.60	28.05	-17.0%
Digital	5.2	6.1	6.5	6.4	11.3	14.8	17.6	20.5	23.0	25.2	17.4%
Downloads	0.7	0.8	0.9	1.1	6.3	9.3	11.3	13.0	14.0	14.4	18.0%
Mobile	3.7	3.1	3.7	3.6	3.4	3.3	3.3	3.2	3.2	3.2	-0.9%
Streaming	0.7	2.3	1.9	1.7	1.7	2.2	3.0	4.2	5.8	7.6	35.2%
Total Recorded Music	121.5	112.8	100.7	91.31	82.5	72.2	65.3	60.5	56.6	53.3	-8.4%
Live Music	54.6	59.82	64.3	68.4	72.9	78.0	83.8	90.3	97.7	106.0	7.8%
TOTAL MUSIC REVENUES	176.1	172.6	165.0	159.7	155.4	150.2	149.1	150.8	154.3	159.2	0.5%

Figure 2 – South African Music Market (EURO Million). Source: PwC Media Outlook 2014 - 2018

The trend is clear: as physical goes down and down, digital takes its place, having almost 50% of the recorded music segment by the end of the decade. For nMusic and TRACE partnership, the industry landscape shows a huge potential market to get into, with the streaming segment presenting a CAGR of 35,2%. There is also space to grow in the download sector, a bigger market than streaming, although presenting a bit lower growth rates. Digital is evolving fast and consumer spending is forecasted to grow on its segments (DMR 2014). There are key drivers of this shift to digital music: constant growth and investments in broadband; fast-tracking smartphone and mobile devices penetration; music is cheaper for the consumer; immediate access and portability. According with DMR 2014, digital music transition in South Africa was headed by the 2012 iTunes entrance. Although, the report emphasizes that in a near future, the increasing accessibility and attractiveness of streaming services, grounded on access to

[14] The music market was worth R2.1 billion in 2014, down from R2.2 billion in 2013, according with PwC.
[15] CAGR – Compound Annual Growth Rate is the ‘the year-over-year growth rate of an investment over a specified period of time’, according with *Investopedia*.

content rather than possession through a download, will be a key driver of digital music evolution.[16]

Potential Partnership Analysis

The proposed partnership will seek to take advantage of this booming digital music phase in South Africa. Following, an analysis of each partner – nMusic and TRACE – will be conducted: nMusic is a 5-year digital content distributor launched in 2010 to build up an innovative music streaming solution, skilled to satisfy the major bodies on the music industry: consumers, artists, publishers and labels. nMusic's partner is going to be the French urban music and sports television channel, TRACE.[17] Launched in 2003 with the support of *Goldman Sachs*, TRACE provides R&B and Hip-Hop music and sports entertainment to a young and young adult audience, between 15 and 34 years old. TRACE has been in South Africa since 2007 with its TRACE Urban channel, and recently with a second channel, TRACE Sports Star, both available on the pay-Tv *Digital Service Television* (DStv, from the media company MultiChoice),[18] which has 5 million paying households (DStv 2014 Annual Report). According with DStv information, TRACE reaches about 2 million TV consumers with its channels. Being present on the South African TV market, the partnership with nMusic will be grounded on TRACE's brand awareness (94% according to our Market Survey) and established presence through a well succeed target penetration.[19] Beyond TV channels, TRACE has available in South Africa its mobile app, country-specific social networks (Facebook and Twitter) and its mobile operation, TRACE Mobile. Regarding nMusic, it shapes the business model according with the partner's goals (private label) and it has relevant international experience, being present in Middle East on partnership with the telecom

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[16] On the Technology Analysis – present within PESTEL Analysis on the *Appendix 4* – further details are emphasized that help understand industry drivers and challenges.

[17] TRACE core business is producing unique content and Pay-Tv channels spread in 162 countries via 39 satellites and 220 carriage contracts In the end of 2013, TRACE had 37 million paying subscribers, an impressive number considering that one year before it had 27 million. *(See TRACE worldwide satellite footprint in Appendix 7).* Their geographical main interest is on the African and Caribbean countries.

[18] Consumers have access to the two TRACE channels by subscribing specific DStv monthly-paid packages: TRACE Urban (channel #325) on the Compact, Extra and Premium packages; TRACE Sports Stars (channel #188) on Extra and Premium.

[19] TRACE operation in South African has had a significant success in terms of target penetration in different segments, winning consecutive prizes as the 'Coolest Music Channel' and the 'Coolest TV Channels' by youth audiences (TV segment) and also having great audience response on its 'TRACE Music Stars' mobile competition with 14 000 three minute auditions entries (mobile segment), receiving positive reviews from media: *The Secret Behind TRACE TV's Seemingly Unbreakable Youth Connection*, 03rd July 2014, http://www.adlip.com/secret-behind-trace-tvs-seemingly-unbreakable-youth-connection/#sthash.0XllgNB8.dpuf (last access on 2014/11/02)

Intigral to build the streaming service *Sultn*; in Angola, creating *Kisom* with the telecom Unitel and in Nigeria building *Zyng*, on a partnership with another telecom, Airtel. In its homeland has an alliance with PT to build MEO Music.

Partnership Strategic Fit

Strategic fit on international partnerships is much of compatibility of partner's agendas and structures (Rugmann, A. and Collinson S., 2008). The authors consider that building a partnership between 2 companies implies two requests: i) a common vision aligned with both sides overall strategies; ii) present synergies and complementarities between each part resources. For nMusic, this movement represents diversifying revenues from its main territory (Portugal); minimizing risk exposure and cost efficiency by entering on a new country with a previously established company; enjoying economies of scale by increasing its library of content at a minimum cost; keep growing on a flourishing continent for digital music, Africa. A common vision might be build upon these individual goals as TRACE pretends to diversify its portfolio, increase product range differentiation from competition, deepen its 360º proposition by being constant in consumer's day-to-day life and enter on a segment where it is not yet present – digital music streaming. According to our market survey, 86% of respondents state that offering a streaming service fits with TRACE TV music channels. Alongside with these elements, there are natural synergies that reinforce the strategic fit of nMusic and TRACE: nMusic flexible business model to display the music platform and TRACE presence on mobile devices with its own app; their value proposition seek an interconnection between its core products and services and the social networks ("sharing" attitude); there is a clear synergy on the music content negotiation, since both companies have to organize and reach agreements with industry players to present licensed products. A synergy can be explored to gain efficiency and increase library content in quality and quantity; TRACE will also gain a way to differentiate from other music TV channels, by being the first one in South Africa with a music streaming service. Further, to strengthen this strategic fit, a Products and Services portfolio for the partnership will be defined.

Partnership Products and Services

The nMusic B2B2C business model (*explanation and graphical representation of this model in Appendix 8*) enables the company to embrace a partnership where all the services it provides appear under TRACE brand name. To establish the suitable P&S offering for the South African customer, our analysis used a market survey conducted to people living in South Africa (*see Survey details on appendix 9*) and market studies from PwC that indicate what customers value and desire regarding digital music and streaming services. After knowing what customers' needs are, an interpretation is performed to match those needs with nMusic/TRACE value proposition. The P&S portfolio of the partnership nMusic/TRACE is presented on Figure 3. The features proposed were corroborated by nMusic executives.

Customer Statement of Need	Interpretation of Needs	P&S Features for South African Market
South Africans need and enjoy Music Diversity **Source: PwC Reports**	As a multicultural country, music styles include local Hip Hop, R&B, pop, choral styles and dance music such as kwaito. American songs are also widespreaded amog young generations.	nMusic has a diverse library of music nMusic (on the partnership in Portugal with PT it has 20 million songs) will complement the TRACE proeminence on R&B and Hip-Hop.
Music has to be present everywhere at any time **Source: 67% of respondents on our market survey state that their willingness to pay for streaming increases with Triple Play (multi-access on TV, computer and mobile handsets) and 62% present the same opinion regarding offline mode.**	The streaming service must guarantee a portable use to answer to customer needs.	nMusic offers a streaming service through a multi-platform system that synch music on computer, TV, mobile phone and tablet. TRACE endorses a 360º experience concept and should keep it for the streaming service: making available a mobile app (using the existing one might be an option); a website where users can download a desktop app; providing the service through TV must be assured as this is an added-value feature offered by nMusic. The offline mode offered is also a good answer to meet this customer requirement.
Advertising is annoying and disruptes music experience **Source: 87% of respondents on our market survey state that advertisment is annoying**	Direct Interpretation	nMusic platform is, and has always been, ad-free.
The connection with Facebook is now key on online services **Source: PwC Reports**	Estimates from "South African Social Media Landscape 2014" report indicate that Facebook as 9.4 million users in South Africa (total population - 54 million). Consumers want to share their lives, activities and experiences.	"Sharing" is one of nMusic values, therefore the platform enables this option on a user-friendly way. TRACE has its own Facebook and Twitter accounts in South Africa, fact that will reinforce the "sharing" need desired by users.
South Africans value video-clips and live concerts **Source: 78% of respondents on our market survey state that their willingness to pay for streaming increases with video-clips available and 89% present the same opinion regarding live concerts.**	Direct Interpretation	Despite not broadcasting live content, nMusic offers music's video-clips on its platform.
Downloading is one of the preffered online activities of South Africans **Source: 92% of respondents on our market survey state that their willingness to pay for streaming services increases with downloads available and 63% state that having more than 15 downloads per month is a good offer**	Music downloads experimented a boom after iTunes entrance in 2012. South Africans value the possess of music. The service will have to offer the posibility of downloading music in order to be competitive while differentiating from other streaming services.	On the partnership with PT (Meo Music), nMusic offers 10 monthly downloads - a unique feature on the streaming landscape - but in South Africa it will have to offer more per month.

Figure 3 – nMusic and TRACE Products and Services Offering

Partnership Mission, Vision and Objectives

We will define a **vision** to the nMusic – TRACE partnership: "*In a five-year plan, to be the digital music leader in South Africa by offering a multiplatform service of streaming that satisfies all the music industry players and is the 1st choice of music consumers"*. Regarding the **mission**, our proposal for the partnership is the following: "*Offering a music experience on a legal and licensed environment that fulfills customer needs, profiles and tastes by being everywhere and available all the time".* To embody the vision and mission, some SMART - Specific, Measurable, Attainable, Relevant and Timed - **objectives** must be defined:

1. Partnership should start its operations until the end of 2015;
2. Have agreements for the service with at least 2 big record labels from the country's big labels - Sony, Warner Music Gallo-Africa or Universal;
3. After 1 year of activity, the new service should have at least 10% (200 000) subscribers of TRACE pre-existing TV channels subscribers (2 000 000);
4. Stimulate brand awareness within TRACE pre-existing subscribers;
5. Have at least a 15 million-song catalogue after 1 year of activity.

Industry Mapping

Reaching objectives depends on the inherent industry dynamics and how the partnership can answer to it, by influence and being influenced by such processes. To assess influence and relevance of stakeholders on nMusic business activities, an Industry Mapping will be conducted, identifying nMusic Clients and Investors, Suppliers and Distributors, Competition, Regulatory Entities and the Original Equipment Manufacturers (OEMs). *Clients* can be divided in terms of B2B segment – where TRACE appears, but our analysis can also point out companies such as the South African telecoms MTN, Telkom, Vodacom[20] or Cell C, or satellite operators (TV packages providers) like DStv or its main competitor StarSat, as potential nMusic clients. Those companies represent the nMusic's mode of entry in South Africa due to the nature of its business model (B2B2C). On the B2C segment, there is the end-consumer of the streaming service for which the service is mainly built. Regarding

[20] Recently, Vodacom reached a partnership with Deezer to provide a streaming service for its clients. (Memeburn, Vodacom, *Deezer tie the music-streaming knot for* South Africans, 10th September 2014. http://memeburn.com/2014/10/vodacom-deezer-tie-the-music-streaming-knot-for-south-africans (last access on 2014/11/18)

Investors, we can identify nMusic's current shareholders, Diligence Capital SGPS Group, Pathena and Explorer Investments because of their relationship on the other missions (Portugal, Nigeria, Angola and Middle East). Recently, the Swedish media corporation Modern Times Group (MTG) acquired 75% of TRACE on a 30 million euro deal[21]. For this reason, we can also target MTG as potential investor for nMusic. In terms of *Suppliers*, due to the type of service that provides, they are only associated with library content – the music – being those who possess or have rights upon music content. Music authors, composers and publishers' rights are managed and represented by the not-for-profit Southern African Music Rights Organisation (SAMRO). Founded in 1961 to protect intellectual property by defending and protecting the copyright laws and acts and assuring that the ones who create content gets its royalties paid. SAMRO current main concern involves digital music – and specifically, streaming services – due to negative effect on music creators of unlicensed and illegal content present on streaming libraries and the correct payment of royalties when a stream is made by the end-user. The Recording Industry of South Africa (RiSA) represents the interests of artists, music producers and record labels. Founded in the 1970s, today it has about 2000 members, including the three major[22] record labels in the country – Universal Music, Warner Music Gallo-Africa[23] and Sony Music Entertainment. Protecting the industry from music piracy, establishing and seeking the reinforcement of a code of conduct and helping the sector to growth in the country are its main objectives. Moreover, it is the official South African representative to the IFPI. Although RiSA welcomes independent labels within its organization, the Association of Independent Record Companies (AIRCO) mainly represents those companies. According to RiSA, South African music market is the only one in Africa that follows the European and North American profile with the clear dominance of the major record companies in terms of recorded music. For nMusic, this might be an advantage since it presents a similar market supplier configuration to one it has to face in Portugal. All these suppliers present an extreme importance for nMusic since it will have to handle

[21] Digital TV Europe, *MTG completes TRACE Deal*, 27th June 2014 http://www.digitaltveurope.net/199982/mtg-completes-trace-deal/ (last access on 2014/11/02).
[22] According to RiSA, Universal, Warner and Sony represent three-quarters of distribution and two-thirds of sales in music industry. Sony is the biggest record label, with its market share fostered by the acquisition of the popular independent record Select Musiek, in 2013.
[23] Warner Music Gallo Africa was established in 2006 as a joint venture between Warner Music Group and the 87-year-old domestic label Gallo Africa.

negotiations and agreements with them in order to build its library. *Competition* is a relevant group since South African streaming market is already a red ocean, indicating that it will face fierce competition. On the next chapter, a detailed Competitive Assessment will be present to evaluate the intensity of competition in the market. The South African *Regulatory Entities* influence both the normal business and the way nMusic relates with its Suppliers and Competitors. The applicable legislation is the Intellectual Property Amendment Act of 2013, a legislative action undertaken by the Government of South Africa that tackles copyright, performers' protection and proprietary trademark. The reinforcement of these rules belongs to the Government assisted by RiSA. Finally, regarding *OEMs* they are an important player, since music – as seen in the Literature Review – is highly impacted by technological advances and nMusic service, an online music platform, depends of the availability and affordability of the system combined with its features. Being aware of the constant transitions and innovations is a way to lead on this challenging and competitive environment. *On appendix 10, this Industry Mapping is schematically presented.*

Competitive Assessment

The South African streaming market where TRACE and nMusic will form a new service has indirect competition (referring to music consumption) and direct competition (companies with similar P&S offering to nMusic streaming service).[24] As indirect competition, we have to consider the still dominant format – CD album – where one retailer – *Musica* – has nearly half of the market.[25] PwC's Media Outlook points out the low penetration of Internet in some areas, more traditional and less urban, as a reason of this success, despite the observed and projected decline on physical sales segment. By now, *Musica* does not have a download store. This format had a tremendous impact on the country's digital market – Apple's iTunes entrance in December 2012 led downloads sales to skyrocket,[26] and as a consequence the value of the digital music market has doubled in just 1 year. Local online stores, such as the telecom operator MTN with its Play Store and Spinlet (on business since 2006) have not

[24] A limitation on our competitive assessment analysis is the inexistence of public music streaming market shares regarding South Africa. According to nMusic executives, this is due to the early stages of the industry in the country.
[25] According to Musica's shareholder, Clicks Group, the company had a 46.2% share of CD sales in 2013 (total revenues on this segment accounted R974 million), an increase up to the 43.7% market share in 2012.
[26] Download-based revenues increased to R86 million in 2013 up from R15 million in 2012, according to PwC figures.

reached the same success and popularity as iTunes, despite some recent pitfalls for Apple's music store as its sales decrease 14% worldwide since the beginning of 2014.[27] The Palo Alto based company has recently acquired on a US$ 3 billion deal the company Beats Electronics, provider of the streaming service Beats Music. So far this will not be a problem to nMusic has this service is not available in South Africa. As indirect competitors, we may also consider Youtube on its current version where users can create their profiles and song playlists and on its future streaming service, announced on 12th of November 2014. Named as Music Key, it will offer second plan reproduction, offline mode and will be available on a premium base with monthly payments. By now there is no official confirmation of when this service will arrive to South Africa. As other emerging markets that experimented huge mobile penetration, South African digital market is also influenced by mobile formats as ringtones (a person can do an added-value call and listen to the chosen song or it can purchase the ringtone). Regarding direct competition for nMusic service, our analysis will focus on the main streaming services available in South Africa. From a monthly price range between EUR 1.80 and EUR 4.40, there are several services that offer online music platform through browser and/or own apps, being also available in mobile devices. Nevertheless, none of them allow the consumer to have access on TV, watch videoclips (nMusic was pioneer on this feature) neither the possibility of downloading songs - 3 features provided by nMusic and largely enjoyed by South African consumers, as stated before (see *Partnership Products and Services* chapter). Another trend on major streaming players is that all are ad-free, reflecting the customer feeling that ads disturb music experience. Next, it is presented a brief description of future nMusic/TRACE main competitors in South Africa:

Rdio - the world's second-largest streaming service (present in 60 countries) was launched in South Africa on December 2013. Displaying a 20 million songs catalogue, it offers a 6-month web browser free trial. To have more extended access there are two alternatives: for EUR 1.80/month the user has unlimited streaming on browser and desktop app; for EUR 4.40/month the service is available on both desktop and mobile streaming, allowing the consumer to synchronize song for offline mode.

[27] Digital Music News, *iTunes Music Sales Down 13-14% This Year*, 27th October 2014. http://www.digitalmusicnews.com/permalink/2014/10/27/itunes-music-sales-13-14-year (last access on 2014-11-19).

The Kleek - specifically conceived for African public, The Kleek was launched in 2013 as result of a partnership between Universal Music Group (UMG) and Samsung. It is entrenched on Samsung smartphones – users have free streaming for 1 year. By now there is no information about the price scheme after this period has expired neither when it will be available on other smartphones. There is no desktop version of The Kleek.

Simfy - the first relevant streaming service in South Africa (it started in 2012). It provides premium streaming for EUR 4.40/month on its package *All Access*, allow customers to save music to listen on offline mode. Its library contains 27 million songs. Simfy also offers a cheaper tier – EUR 1.80/month – that enables users to have access through a browser or desktop app (no mobile offer). They innovate in terms of price arrangement by introducing an annual payment for its *All Access* tier where users pay EUR 45.30/year in advance (saving EUR 7.30 over the monthly schedule). As stated before, in June 2014, Simfy reached an agreement with the telecom MTN and now the latter's subscribers can have the *All Access* at a cheaper rate, EUR 3.60/month.

Rara - Launched in the end of 2012 with a 22 million songs catalogue, this streaming service distinguishes from the competition by offering a different pricing scheme: without any trial version, users pay EUR 0.51/month for access on browser (there is no desktop app) or EUR 1.02/month with the mobile platform involved. But these extremely low prices are only applied for the first 3 months. After that, the prices will be higher than the ones practiced by Rara's competitors: EUR 2.50/month on the first case and EUR 5.05/month for the premium tier (offline mode is an exclusive feature of this tier).

Deezer - The French company offers the bigger catalogue of songs in the streaming segment – nearly 30 million songs. The company targets mainly the smartphone users, presenting a popular mobile app while on desktop users only have the service through a browser. The price scheme is similar to the one used by Simfy and Rdio – unlimited access for EUR 4.40/month on all devices while EUR 2.20/month will grant you access to the web browser. There is a free mode – the only streaming company doing so in South Africa - where Deezer provides users 2 hours of music per month. As pointed out before, on October 2014, it reached an agreement with Vodacom to provide the Premium offering for the telecom subscribers free of charge during 1 month. After that, they will pay EUR 4.40/month. For Deezer it is a good opportunity to grow as Vodacom as around 32.5 million subscribers.

We should also add that Spotify – the worldwide market leader on streaming considering revenues – and Pandora – an American web-radio that selects songs to customers according to their prior feedback – are not yet available in South Africa, despite efforts of both to enter on a near future. By now, this fact represents a positive hint for nMusic. The level of competition is evolving fast as it can be seen by the player's moves and strategies (partnership with other sector companies is the market trend). Everyone is trying to attract and preserve customers as much as it can due to the booming phase of the industry in South Africa. *On appendix 11, a table is presented with a comparison of features, prices and characteristics of these services and with nMusic/TRACE P&S offering.*

5 Forces of Porter

After assessing industry attractiveness, mapping key stakeholders and evaluating the level of competition by analyzing main competitors, the Michal Porter's 5 Forces framework[28] will be used to understand the impact of industry structure on nMusic profitability. The framework identifies these forces:

- *Threat of New Entrants* is **High**, meaning that are low entry barriers on the market due to the reduced fixed costs required, limited switching costs and the easiness to establish deals with record labels (for ex. it is relatively easy for Spotify to enter on the market);

- *Threat of Substitutes* is **Medium** since there are several channels and services that can substitute nMusic's platform to listen music, such as Youtube, TV music channels, download stores as iTunes, CD albums sold by *Musica*. The threat is medium since none of these presents the same type of performance and experience while using the service as nMusic one.

- *Bargaining Power of Suppliers* is **Medium** because record labels need companies as nMusic to have their songs on the legal distribution and diminishing losses erasing from

[28] Published in 1979 by Michael E. Porter on the prestigious Harvard Business Review (HBR) magazine, this framework started a revolution on strategy issues, specifically in terms of understanding the drivers that sustain companies' competitive advantage and the impact of industry factors on their profitability and competitive position. The version of the Porter 5 forces used on this work is the one published by Porter in HBR on a 2008 article "*The Five Competitive Forces That Shape Strategy*".

piracy. nMusic has already agreements with major labels – the ones that also lead in South Africa - but they can increase their prices and commissions.

- *Bargaining Power of Buyers* is **High** because TRACE is essential for nMusic entry mode in the market, it is their only client/partner and therefore the revenues coming from South Africa will mainly rely on TRACE.

- *Competitive Rivalry* is **Medium** due to the existence of some international and recognized streaming services, several indirect competitors and considering the fact that there are not high exit barriers. Moreover, illegal downloads impact the streaming market structure by decreasing the number of people willing to subscribe these services.

As a sum up of the 5 Forces of Porter, the industry structure appeals to new entrants, as nMusic, but after its establishment it will pose some risks. The bigger threat to nMusic profitability is the high threat of new entrants (create pressure on prices and costs). Having TRACE doing big efforts on promoting the streaming service, as a legal and licensed catalogue with quality and quantity to reach as many people as possible creating a "customer network" (Porter, M. 2008), and backing nMusic on supplier negotiations in terms of content, leveraging its power against labels – it will generate higher entry barriers and protect nMusic position in the South African streaming music industry.

Competitive Advantage Assessment – VRIO Framework

Resource	Valuable	Rare	Difficult to Imitable	Organized	Competitive Implication
Team - Knowledge, Skills and Background	YES	YES	NO	YES	Temporary Comp. Advantage
Organizational Culture and Structure	YES	YES	NO	YES	Temporary Comp. Advantage
Music Platform - Design and Attractiveness	YES	NO	NO	YES	Competitive Parity
Technology Features (Automatic Cache and Triple Play)	YES	YES	NO	YES	Temporary Comp. Advantage
Sales and Distribution Management	YES	NO	NO	YES	Competitive Parity
Supplier Relationship Management - Reputation and Negotiations	YES	NO	NO	YES	Competitive Parity
Business Model and Partnership Management	YES	YES	NO	YES	Temporary Comp. Advantage

Figure 4 - nMusic VRIO Framework

To assess which nMusic's resources and capabilities provide a competitive advantage for the company vis-à-vis its main competitors in South Africa, the VRIO framework[29] was used, as presented on Figure 4. The table above presents the resources of nMusic

[29] The VRIO framework was introduced on Jay Barney's article 'Firm Resources and Sustained Competitive Advantage', published in 1991 on the Journal of Management. It is a qualitative model that only assesses company resources on an individual basis, not considering the integration of resources.

anchored by organizational systems, technological infrastructure, process and values. It can be identified as sources of competitive advantage, the team's knowledge and skills on music, IT and digital music trends due to decades of work within this field; the way nMusic is organized as a flat team; the flexible business model tailored to answer to TRACE and the ability to manage a partnership by offering constant support to the partner requirements, making adjustments demanded and solving any tech problem that end-users may have while using the service. This will be crucial to build an environment that South Africans enjoy for listening music (being attracted to this platform and avoid illegal music distribution). Although, so far they guarantee a competitive stance for nMusic, they are not totally impossible to imitate and since the company is a start-up it is hard to already identify them as providing a sustainable competitive advantage. Regarding the team, creating processes and an internal cultural environment is crucial to thrive on a disruptive landscape.[30] To improve the partnership and business model, a database for potential partners would be a good solution to enjoy sustainability on the B2B2C model. Regarding technological features – such as automatic[31] cache or triple play[32] - they have also a tremendous value, are rare and very well organized in the company's P&S offering, but they only provide a temporary competitive advantage since it is not hard to imitate. The platform, the distribution channels and the supplier relationship are all valuable resources, but do not unique and relatively easy to imitate, putting nMusic in parity with other players. From the VRIO framework, some general conclusions about the necessary adaptation of these resources on the partnership with TRACE can be extracted: nMusic must employ people who strategically fit with the current staff in terms of understanding the music industry, the streaming paradigm and with great IT skills; adjust the service according to TRACE goals and with the stage in the industry lifecycle in South Africa[33] while preparing the future on a medium/long term, as markets evolve fast; to improve some resources, such as the relationship with suppliers in order to create solid relationships; invest in R&D due to the innovative nature of the service must be a concern too.

[30] The London based company IDEO would be a good benchmark of how to encourage innovation by using internal processes, such as the team brainstorming, storytelling or the organizational memory applied by its employees. The IDEO examples is a good one to follow as it is highly focused on customer needs and behavior.
[31] This feature allows users to have access to its listening history (organized by days), even when offline.
[32] Combining data, voice and multimedia, enables users to sync information in different devices: computer, TV, smartphones and tables.
[33] The data available – see Figure 2 – indicates that streaming segment in SA will be constantly growing until the end of this decade. After 2020, streaming will probably enter on a more mature phase and new innovations might appear.

Partnership Value Chain

To assess which activities are most valuable for the partnership in South Africa and help to build a competitive advantage, a Porter's Value Chain framework was used. nMusic will have responsibility on two primary activities – music content management and technology/service development. These are very important activities on the service and essential for nMusic, since the market recognises its capacity on it. The other activities, such as customer relationship management, sales (within it is revenue collection) and marketing are primary responsibility of TRACE. nMusic will endorse a special coordination with TRACE regarding marketing management. Financial, HR and infrastructure management are considered to be support – or secondary – activities on the partnership. On figure 6, the nMusic/TRACE Value Chain in SA is graphically presented.

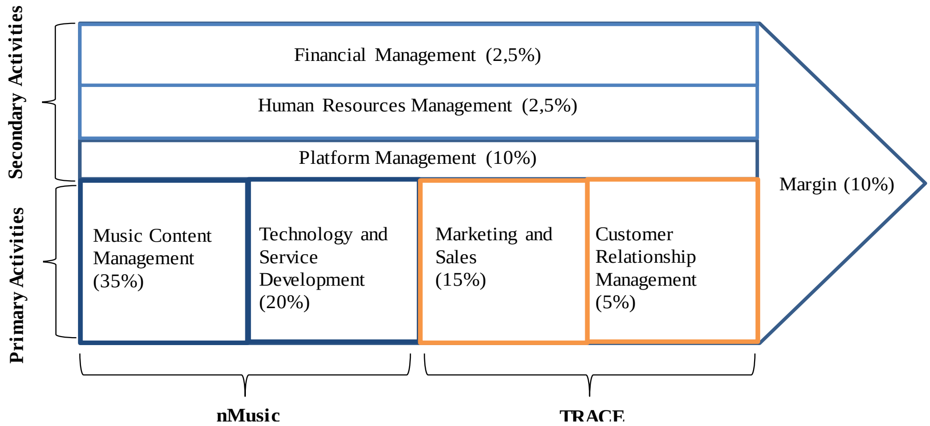

Figure 6 – Diagram of the partnership Value Chain

Building a Profitable Partnership: Revenue and Cost Structure

nMusic and TRACE must create a revenue model that allows to grow the subscription base, attracting consumers from piracy and gaining share on a growing streaming segment. On streaming market, the main challenge is which business model should be used in order to attract paying subscribers. 3 scenarios regarding streaming business models were proposed by nMusic executives and analysed on this work project:

- Freemium: freebase tier with advertisement and a paid premium tier without advertisement (users can upgrade from free to premium);
- Standalone: no ad-service, all paid, usually with different tiers
- Bundle: no ad-service, used on partnerships with other brands – telecoms, for example – where a user has access to streaming by paying other service (telecom package) or if it is customer of a certain company (bank customer).

Our analysis rejected bundle since it is difficult for TRACE to have a service where it has the responsibility of collecting revenues, since in South Africa the company has no experience on that because consumers pay to DStv to have their channels.[34] In terms of rejecting freemium, the reasons are based on the primary market research where consumers feel that ads are annoying. Further, nMusic has no experience on freemium since none of its partnerships uses this model. It is also our believe that freemium is a good model to attract consumer base, but very difficult to be profitable since consumers do not perceive a true value on switching to premium, as Spotify shows, leading the press to state "the more they grow, the more they loss" (PrivCo Media). According to Spotify annual report, the service has 50 million worldwide users, only 12.5 paying subscribers generating revenues of 747 $US million in 2013 and a net loss of 80 $US million. Therefore, our choice goes to the standalone model – it will have different tiers, all paid. This proposal had in consideration the prices practiced by the competitors; the payment and packages timeframe most adopted in the country for subscription services; the value-for-money, since the features available provide efficiency and effectiveness on the acquisition; the availability of features that South Africans most value like downloads, offline mode, video clips; not displaying advertising since it is not well received. Furthermore, market survey results were used to define Standard and Premium Plus package prices (see "*Reasoning*" on figure 5). Features escalate the prices in order to attract users to the categories above. Adopting this revenue structure will assure the attractiveness of the service in terms of pricing by matching the customer needs with the offer. Our price scheme proposal is presented on the following figure:

Package	Price Range	Main Features	Reasoning
Standard	EUR 2.20 / Month	Desktop App only, with offline mode but no downloads and no videoclips	Targeting low cost users on similar price to the one offered by Rdio, Simfy and Deezer, but with one extra feature compared to them: the offline mode. **Market Survey: 51% of respondents stated that this price is adequate for the package offering.**
Premium	EUR 4.50 / Month	Muti Devices access, all features included	Tageting premium offers from competitors, with several extras: TV access, video-clips and downloads. Granting the possibility of downloads is a way to compete with the successful iTunes.
Premium Plus	EUR 5.50 / Month	Muti Devices access, all features with 20 downloads	This offer goes beyond competitors best packages by offering all the features and the possibility of downloading 50 songs per month (same point regarding iTunes). **Market Survey: 56% of respondents stated that this price is adequate for the package offering.**

Figure 5 - Price Scheme of nMusic/TRACE Streaming service

[34] nMusic and the Portuguese telecom PT offer a bundle model for the MEO Music streaming service to PT customers (On paying certain telecom packages, the streaming is offered and music perceived as free). For non-customers, MEO Music is a standalone service.

For this partnership, it is proposed the usage of a shared-costs approach between nMusic and TRACE, dividing on a 50-50 basis the net profit, a model that fits nMusic executives' ambitions. It is the appropriate since the current TRACE potential customer base is 2 million people, assuming the number of people with access to their TV channels. Moreover, nMusic has experience with it on partnerships where the expected reach is around hundreds of thousands – the goal is to have 100 000 users after 6 months and in 1 year of activity, have 200 000 users (represents 10% of TRACE customer base).[35] Following it is presented a cost structure assuming the revenue of one user, presenting the major costs[36] (corroborated by nMusic executives) to calculate the net profit per user:

Standard	Premium	Premium Plus	
2.20 €	**4.50 €**	**5.50 €**	Revenue per user
0.31 €	0.63 €	0.77 €	VAT on Digital Goods (14%)
1.89 €	**3.87 €**	**4.73 €**	
0.24 €	0.48 €	0.59 €	Fee to SAMRO (12.5%)
1.66 €	**3.39 €**	**4.14 €**	
1.16 €	2.37 €	2.90 €	Fee to Record Labels (70%)
0.50 €	**1.02 €**	**1.24 €**	
0.03 €	0.06 €	0.07 €	Bandwith cost (6%)
0.47 €	0.95 €	1.17 €	Net Profit per User
0.23 €	**0.48 €**	**0.58 €**	nMusic Net Profit per User

Figure 6 - nMusic/TRACE Cost Structure

It is assumed the structure presented by nMusic executives, information gathering on the market (VAT on digital goods) and industry analysis (fee to SAMRO) and on nMusic 2013 Annual Report to know how much music licenses from record labels cost *(see the nMusic 2012 and 2013 P&L on Appendix 12*). Regarding bandwidth costs, nMusic pays for the capacity of data in the network. It is a variable cost depending on the number of active users. For example, with 200 000 paying users, only 80% can be frequently active users and nMusic will pay according to this group, because the capacity of data paid is based on the real data used. According to nMusic executives, for our customer base the cost will be around 6%, the value assumed. A scenario-analysis

[35] In Angola, on its partnership with Airtel, nMusic receives a royalty on revenues, since it is expected to quickly (1 year) achieve more than 1 million users. nMusic executives state that only on those conditions they can assure a deal with a revenue royalty, usually around 20%. For smaller operations as this one with TRACE in South Africa, the shared cost and revenues is the more suitable approach.
[36] Staff and other operating costs for nMusic were intentionally left out of our analysis as they represent an insignificant part when compared to the major item – music licenses – as they highly impact the profitability.

was conducted to observe the potential of this revenue-cost structure with the standalone business model, assuming the costs and the number of subscribers presented before to end up with a potential net profit. Our analysis undertook 3 scenarios - the Best, the Most Likely and the Worst. The big difference among them is how users allocate themselves by package, reflecting the capacity of moving customers towards more Premium packages. On the Best case, it is assumed that Premium Plus will be the most chosen one. On the Worst case, the service fails to sell its premium offering and consumers stay mainly on the Standard subscription. On the Most Likely scenario, it is assumes a kind of Normal Distribution with the majority falling on Premium and two smaller groups, one on the left (Standard) and one on the right (Premium Plus). The following figures present the Most Likely Scenario with the correspondent monthly revenue for nMusic (*all the scenarios are listed in Appendix 13*):

Month	TOTAL USERS	STANDARD USERS	% ON TOTAL	PREMIUM USERS	% ON TOTAL	PREMIUM PLUS USERS	% ON TOTAL	Monthly Net Profit for nMusic
1	16600	2490	15%	11620	70%	2490	15%	7,582.40 €
2	33200	4980	15%	21580	65%	6640	20%	15,340.94 €
3	49800	7470	15%	29880	60%	12450	25%	23,275.60 €
4	66400	9960	15%	36520	55%	19920	30%	31,386.39 €
5	83000	12450	15%	41500	50%	29050	35%	39,673.32 €
6	99600	14940	15%	49800	50%	34860	35%	**47,607.98 €**
7	116200	23240	20%	58100	50%	34860	30%	53,508.34 €
8	132800	26560	20%	66400	50%	39840	30%	61,152.39 €
9	149400	29880	20%	74700	50%	44820	30%	68,796.44 €
10	166000	33200	20%	74700	45%	58100	35%	77,321.14 €
11	182600	36520	20%	91300	50%	54780	30%	84,084.53 €
12	199200	39840	20%	99600	50%	59760	30%	**91,728.58 €**

Figure 7 – Monthly Net Profit for nMusic on the Most Likely Scenario

With our assumptions, the service would end up its first year with the referred 200 000 users, 50% of it Premium, 20% Standard and 30% Premium Plus. With the price scheme chosen and the current cost structure, on the end of 1st year the ***net profit for nMusic will be 91,728.58€ monthly*** (the same for TRACE). To improve the service profitability, music licenses have to be tackle with the South African big 3 record labels - Universal Music, Warner Music Gallo-Africa and Sony Music Entertainment. If gains are obtained on negotiations with them, profitability will be positively impacted. All the efforts should be putted on this challenge.

SWOT/TOWS Analysis

After a deep external and internal analysis of nMusic/TRACE partnership, a SWOT/TOWS analysis was conducted to identify strategic options for nMusic and take advantage of arising opportunities, use of strengths, diminish weaknesses and avoid threats. On the next figure, a SWOT/TOWS analysis is presented.

SWOT/TOWS ANALYSIS	Strengths	Weaknesses
	1 - Unique and flexible business model able to partner with large companies 2 - Team with deep music knowledge, background and able to negotiate with key music players 3 - Service available in multi devices, overcoming competitors 4 - Only uses licensed and legal content 5 - Well designed and user-friendly music platform, constantly improved by customer feedback 7 - International track (Middle East, Nigeria and Angola)	1 - Dependence of only one client (TRACE in South Africa) 2 - Limited brand awareness 3 - High dependence of record labels 4 - Limited financial resources 5 - No direct knowledge of South African music industry
Opportunities	**SO Strategies**	**WO Strategies**
1 - Steaming segment is the fastest growing within South African music industry 2 - No presence of Spotify or Pandora 3 - High smartphones penetration and keep growing 4 - Possibility of expanding with TRACE to other African markets 5 - South Africans reacted very well to music downloads on a legal environment	→ Establish the partnership and launch the service as soon as possible to take advantage of Spotify absence → Constant improvement of mobile app → Present always one or two features that competitors do not have to enhace differenciation → Ask customer feedback to improve the easiness of using the platform	→ Use the limited brand awareness to surprise competitors and jeopardize the opportunity to grow on this segment → Create a partnership with other streaming and digital music companies to pressure record labels → Establish network with investors (private equity companies) → Hire staff with deep knowledge of South African music industry → Be always available to meet TRACE requirements in order to eliminate potential sources of conflit, allowing the partnership to expand
Threats	**ST Strategies**	**WT Strategies**
1 - Piracy rates (represent 25% of music industry revenues) 2 - Consumers value downloads before streaming 3 - Big 3 labels dominate the record market 4 - Awareness of streaming is still limited 5 - Competition on digital music starts to be intense and it is easier for them to imitate nMusic best service features	→ Establish institutional partnerships to fight piracy, mainly on younger audiences → Convince TRACE to campaign for the access of music, rather than the possess of music by promoting the platfrom as a space that also has downloads → Use the growing streaming segment to increase bargaining power on negotiations with record labels → Use TRACE resources and channels to promote streaming → Answer to the competitors with advanced features and innovations	→ Strong awareness of TRACE will minimize the risk of entering on a market where streaming is still on the beginning → As TRACE is already on music industry, use their network to build relationship with key players (record labels and right holders associations) → Increase bargaining power while negotiating with TRACE by arguing the advantages of a fast entrance on streaming

Figure 8 – SWOT/TOWS Analysis

Mode of Entry and Collaborative Arrangement

One way to minimize or avoid threats involved on entering in the South African market is to get into a partnership with a local or previously established company.[37] This entry mode will allow the company to increase the probability of success by reducing costs, gain specific market/industry knowledge and network, it overcomes legal and governmental constrains, diminishes the intensity of competition and minimizes nMusic's exposure to a potential risky environment. As it was stated before, the

[37] This strategic option follows a recommendation made by a representative of *AICEP*, a Portuguese state-owned that seeks to attract foreign investment to the country and helps to internationalize Portuguese companies, and also by the *Portuguese South African Chamber of Industry and Commerce* (CCILSA) that provide country-specific presentations and internalization guides to the purpose of this work.

partnership to establish will be with the TV channel network, TRACE (an innovation to nMusic since so far they only did partnerships with telecoms). Regarding staff to support the partnership, nMusic has currently 30 people on its team divided between Lisbon (managerial positions and content management) and Oporto (technical and data staff) and when abroad nMusic has always no more than 2 people on one country, one to the marketing coordination with the partner and another one that will fix content management negotiations and agreements with music suppliers and key stakeholders. For this partnership, a similar strategy might be followed as a learning curve with this organizational structure in international partnerships starts to be matured within nMusic. TRACE will use their staff in South Africa[38] but the main resources for this partnership – as nMusic will build the service – will go to stimulate TRACE's brand awareness, marketing channels and sales processes. In terms of collaborative arrangement, the partnership must be operative through a technology licensing approach (non-equity): as defined by Rugmann and Collinson (2008: 42), a license is a contractual arrangement in which one company, in this case the licensor nMusic, offers access to some of its core assets – technology materialized on the music platform and the content library agreed with labels, publishers and music creators - to another company, in this case the licensee TRACE. This type of arrangement, according with internationalization theory must be held for a period of 5 to 7 years (Rugmann, A. and Collinson S., 2008) and our analysis propose that a partnership evaluation must be conducted five years after its release. After that, nMusic and TRACE must have the option to extend if it is their will. Following this arrangement will guarantee that nMusic does not loose its control the firm specific advantages (tech infrastructure and music content negotiation) while it avoids an unnecessary significant exposure to an unknown market and environment. Moreover, it is a helpful way to spread the costs with R&D and to add an extra income to monetize the expertise of nMusic service and team. This strategic alliance between nMusic and TRACE will demand both companies resources commitment to fulfill the SMART objectives stated before.

[38] According to the company's press presentation, TRACE has 80 employees divided by specialized areas, like music, sports, marketing, digital media, distribution and also corporate management positions. In South Africa, staff is around 4 to 6 permanent people. The key person is the CEO and founder, Olivier Laouchez (has 25% of the company).

Main Risks, Conclusions and Final Recommendations

Internationalization processes present levels and dimensions of risks that are higher than the ones faced by a company on its original market (Rugmann, A. and Collinson S., 2008). nMusic will face several risks in South Africa, some arising from the market and industry conditions and others due to the nature of the entry mode and collaborative arrangement with TRACE. On the following figure, a Risk Assessment is conducted, identifying the major risks for nMusic, with type, expected impact, its likelihood and the time frame. For each risk, Key Performance Indicators (KPI) were selected and strategies are recommended to overcome those risks.

Risk	Type	Impact (1-5)	Probability	Time Frame	KPI	Recommendations
Low Streaming Awareness	Commercial	4	Low	Short Term	-Subscribers to streaming services - Market Research	nMusic has to guarantee that TRACE promotes the service
Music Downloads keep the dominant presence	Commercial	3	Very High	Short Term	- iTunes penetration, rate of success and profitability	The service should be promoted stressing that it is the only service in South Africa that offers the possibility of download songs.
Spotify and Pandora entering on the market	Commercial	5	Very High	Short Term	- Market Research	Constantly developing the service and its features to keep the advantage of entering first.
Record Labels increase their fees	Commercial	4	Medium	Medium Tem	- Success on the negotiations - Number of agreements	Readjust the price scheme of the low and medium tier (costs driven price strategy).
Music piracy increases	Cultural	2	Medium	Medium Tem	- Number of illegal download platforms - Data of music piracy	Raise awareness for the legal music environment and partner with associations and authorities to campaing against piracy.
Partnership with TRACE fails	Partnership	5	Low	Long Term	- Profitability for TRACE	Seek a rapid growth and promote a good relationship with TRACE but prepare a plan to look up for other investors and partners.
Lack of commitment and financial support by TRACE	Financial	4	Low	Long Term	- Investments of TRACE on the service development - Marketing campaigns	Prepare other alternatives for revenue streams, such as allowing advertisements on the platform
High dependence from the leader Celestino Alves	Organizational	3	Medium	Short Term	- Decision power of other team members	Empower other team members with more responsability
Failing to achieve SMART objectives	Partnership	4	Low	Medium Tem	- Number of Subscribers to the service - Revenue streams - Market share	Readjust expectations created before entering on the market, follow the best market strategies conducted by competitors and invest hard on a good music library
Exchange rate fluctuations (EUR - Rand)	Financial	2	Medium	Medium Tem	- Inflation rate - Fluctuations of Rand	Increase revenue streams from other regions and markets where nMusic is already present.

Figure 9– Risk Assessment for nMusic entrance in South Africa

The general conclusion of this Work Project is that the nMusic entrance in South Africa must occur as soon as possible. On a summary, these are the main reasons: the industry momentum is the adequate with high rates of growth expected for streaming; by now there is only one big competitor in the country (Deezer) and entering before Spotify and Pandora can leverage its position to attract and retain consumers; the chosen partner TRACE enjoys a very good reputation on the typical first streaming target (urban youth and young adults); TRACE has a track on the music industry due to its music TV channels and this knowledge and network will be useful to negotiate music licenses; displaying a streaming service is a coherent movement for TRACE, strategically fits with the other company services and allows to fulfill their goal to be a 360º firm able to satisfy consumers with a wider range of services and products; for TRACE entering on a B2B2C model will prevent the launching costs to be very high because the service development will be nMusic responsibility while marketing will be TRACE main task (a key strength on TRACE, since they present a good track on target penetration with high levels of awareness and being recognized with public awards and prizes); for nMusic a technology licensing agreement is also very financially attractive as this solutions does not involve significant resources; according to our Most Likely Scenario, the service will generate positive net revenues for both companies. Despite this, the service will also face some relevant challenges, such as the high costs of music licenses; the big presence of iTunes shifting consumers to music downloads; the ways of doing business are different from Portugal to South Africa and from TRACE to nMusic; an economy that despite its growth and development suffers from high structural unemployment, significant disparities on income and a persistent inequality that crosses all the country with consequences on disposable income. Another challenge – and threat – to the service is the digital music piracy that in 2013 accounted for 31% of industry revenues. Tackling this number down will mean more consumers to legal and licensed content can signify extra-revenues and profits. nMusic/TRACE can fight this problem by allowing consumers to download songs on their platform, a feature that any of its competitors presents and will differentiate the service on the same time that offers to illegal download users an opportunity to shift to a legal service. It is also important that nMusic keep its expansion ideas to other markets, as it will help to financially support the company, diversifying revenues from Portugal at the same time that prevents an international venture in one country that may end up on a failure or withdraw. These are the general conclusions and challenges regarding the internationalization strategy of nMusic to enter on the South African music streaming market on partnership with TRACE.

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ENTERING IN THE SOUTH AFRICAN MUSIC STREAMING MARKET - INTERNATIONALIZATION STRATEGY OF NMUSIC

ALEXANDRE DAMASCENO DA SILVA POÇO

#1472

BOOK OF APPENDIXES

A Project carried out on the Field Lab in Entrepreneurial Innovative Ventures, under the supervision of:

Professor Filipe Pamplona Castro Soeiro

7th January 2015

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Appendix 1 – Recorded Music Transformation to Digital

The graph below shows the decline in the recorded music business since the late 1990s. A major conclusion to take is that the fast weakening is not justified by a decrease in music consumption or interest but to a shift in consumer's behaviour to digital formats, in this case, music downloads.

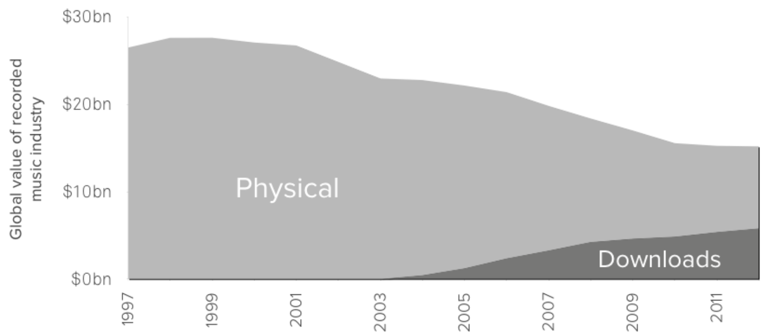


Figure 1 – Music Industry Transformation (Source: Spotify website)

Appendix 2 – Key Macroeconomic Data of South Africa

Our market analysis considered different macroeconomic figures to extract the general conclusions made on the main work project text: GDP is growing after the 2008/09 turmoil (GDP per capita starts to raise again, reflecting the South African's purchase power recovery after several years falling). On the public economy, despite the increase on government's spending in the last years – public servants salaries and social entitlements were increaded – the International Monetary Fund concluded in October 2013 (Report *South Africa 2013 Article IV Consultation*) that the country's public debt is sustainable on the long term considering the growth projections and the financing needs fpr the upcoming years. Below, it is presented a table with key macroeconomic indicators of South Africa.

					Projections	
	2011	2012	2013	2014	2015	2016
GDP per Capita (€)	6,277.45	5,896.41	5,369.25	5,298.21	6,128.10	6,568.07
GDP Growth Rate (%)	3.6	2.5	1.9	2.3	3.7	4.4
Inflation Rate (%)	5.0	5.7	5.8	5.9	5.1	5.1
Public Deficit (% of GDP)	-3.7	-4.6	-4.1	-4.4	-3.8	-3.3
Public Debt (% of GDP)	39.6	42.3	43.8	45	46.1	46.8
Current Account Balance (% of GDP)	-2.0	-5.2	-5.8	-5.5	-4.7	-5.1

Figure 2 – South Africa Macroeconomic Figures and Projections (Sources: EIU, IMF, South Africa Statistics and Trading Economics)

In terms of wealth creation, South Africa GDP (Gross Domestic Production) can be presented as:

GDP - Composition, by end use as of 2013

Household consumption: 63.8%
Government consumption: 24%
Investment in fixed capital: 22%
Investment in inventories: -0.8%
Exports of goods and services: 30.6%
Imports of goods and services: -39.6%

GDP - Composition, by sector of origin as of 2013

Agriculture: 2.6%
Industry: 29%
Services: 68.4%

Source: CIA (The World Fact Book)

Appendix 3 – The Unemployment Challenge

A major challenge for South Africa's development is its high unemployment rate, being one of the main drivers of the income inequality. The International Monetary Fund (IMF) emphasizes that unemployment is especially high amongst black youth (16-30 years) community coming from low-income families. Despite the growth of GDP per capita, high unemployment rates represent a lag on the country's emergence as a new developed economy. For international companies that are on the frontline to enter in South Africa, this data represents an additional risk as it prevents the consumer to have higher levels of disposable income to spend on services, such as music.

Following, we present the unemployment rates over the last years.

	2009	2010	2011	2012	2013	2014
Unemployment Rate (%)	24.0	24.9	25.0	25.2	25.3	25.5

Figure 3 – South Africa Unemployment Rate (2009 – 2014). Source: IMF

We can observe the dimension of this challenge, by observing that high levels of jobless people are a trend with more than 10 years, as presented on Figure 4:

Figure 4 - South Africa Unemployment Rate on an extended timeframe 2000 – 2014. Source: Trading Economics.

Appendix 4 – PESTEL Analysis

To track the environment that nMusic will face while operating its streaming service with TRACE, a *P*olitical, *E*conomic, *S*ocial, *T*echnological, *E*nvironmental and *L*egal analysis was conducted:

<u>Political Analysis</u>

After the segregation-based regime *Apartheid* (1948 – 1994), South Africa held its first universal suffrage elections in 1994. The key person was Nelson Mandela that after being imprisoned for 27 years was released in 1990 and managed to get a deal with the President Francis de Klerk to end up the white minority rule and state-backed racial separation and create a new democratic constitution. His African National Congress (ANC) became the dominant party after the 1994 election, controlling the parliament and Nelson Mandela was the first post-apartheid President. In 1999, the second free elections expressed the even bigger control of ANC on the legislative and executive power. The National Assembly has chosen the Deputy President Thabo Mbeki to be the next President, succeeding Mandela. After gaining the reelection challenge in 2004, Mbeki was expected to serve until 2009, but end up resigning one year before. Some political theorists and analysts state that ANC continuous command is due to their role on fighting Apartheid. From 2009 until now, Jacob Zuma (ANC) has been the

President. In 2014, he held a big majority on the elections, defeating the opposition Democratic Alliance (DA) candidate, Hellen Zille with an expressive 62% to 22,5% of voting. Beyond the parliament, there is a higher legislative organization – the National Council of Provinces where the governments of the country's 9 regions choose their representatives. Politically, the country is stable due to the big ANC dominance and despite some concerns on the international community [39] after Mandela's death (December 2013) there were no incidents or relevant happenings able to threat the political regime stability.

Economic Analysis

The entry of South Africa in the BRICS group is the formal recognition that the country is the power of sub-Saharan Africa. Moreover, the influence and the ease of access to 15 countries of the SADC (Southern African Development Community), which has more than 250 million consumers, gives it an important role as a platform for other markets in the region. The country also benefits from the fact that many multilateral organizations have regional offices in its territory (World Bank, African Development Bank and UNOPS - United Nations Office for Project Services), being the great centre of multinationals operating in Africa.

South Africa is a middle-income economy, an emerging market with a rich quantity of natural resources. It is the biggest economy of Africa and for many, an example for other sub-Saharan countries as a development model. The key sectors - legal, financial, communications and technologic, energy and transport - are well established and has a stock exchange that is the world's 16th largest, reflecting the capacity of attracting foreign investment to the country. The usual unsteady energy supply outside urban areas delays development on secondary regions. Despite this, the distribution of goods is easily done through the road and rails, assuring the efficiency on the country's day-to-day business. Inequality – one of the world's highest – and poverty are also huge challenges for the upcoming years.

For 2015, the country is expected to grow 3.7% due to an increase on consumption and investment, despite the low growth worldwide. According to IMF, the strengthening of

[39] *Canada News,* Many fear South Africa without Mandela would be a place of violence and suspicion. 26th June 2013http://www.canada.com/health/Many+fear+South+Africa+without+Mandela+would+place+violence+suspicion/8571665/story.html (last access on 2014/12/03). This article was published 6 month before the death of the iconic President Mandela.

business activity will boost the creation of jobs, which will push up domestic consumption, supported by improving the conditions of the black middle class. The new power plants and transport networks should raise the GDP in 2016 and 2017, to 4.4% and 4.7%, respectively. It may, however, decrease in 2018 to 4.0%, with the decline in private consumption as a result of rising interest rates, also linked to the continued deficit in the external account. According with Financial Times, a moderate domestic demand and a sound monetary policy will help to contain inflationary pressure. To the Economist Intelligence Unit (EIU), on the next 5 years the average annual rate of inflation is expected to meet 3.6%, set by the Central Bank. In 2014, this indicator should be set at 5.9%, due to the impact of a weak currency in import prices, particularly in the oil and the increase in tariffs for electricity and wages (IMF, Report *South Africa 2013 Article IV Consultation*). For 2015 and 2016, the average annual inflation is expected to stand at 5.1% (South African Reserve Bank), due to an expected moderation in commodity prices. The Reserve bank also states that further increases in energy prices will lead, in 2017-2018, to a new rise, this time by 5.8%.

In the medium term, the South African government policy will focus on economic growth, maintaining stimulus to growth, including control of the budget deficit and a weak currency, not forgetting macroeconomic imbalances and mitigating the risks associated with the weakness of the economy global. The management of public finances will continue strong, although the rise in the debt service leaves less room for manoeuvre to pursue a countercyclical fiscal policy. The rise in the deficit implies an increase in public debt, especially in the domestic market, even though the previous policy of prudence means that the country can support more debt, subject of confidence from investors (IMF, Report *South Africa 2013 Article IV Consultation*). The public debt, according to the IEU, is expected to remain below 50% of GDP, i.e., a moderate level. However, the constant increase in the debt service and the need to protect investor confidence strengthen in the medium term, the urgency of a deeper fiscal consolidation. The South African Government will face difficult decisions in the face of increasingly pressure to invest in infrastructure, expand social security and increase wages. In this scenario, the EIU forecasts that the budget deficit gradually go down, from 4.4% of GDP in 2014 to 3.3% in 2016 and 2% of GDP in 2018.

Social Analysis

Archbishop Desmond Tutu coined South Africa as the "rainbow nation" due to its diverse and multicultural landscape, being one of most diverse countries on Earth. On a country with more than 54 million (2014 official numbers by South Africa Statistics), the more urbanized areas reflect perfectly this point, as different ethnic and cultural groups share the same areas: black people, Indian (Tamil and Urdu speakers), Chinese and European (like the Afrikaners, Dutch descendants, or the British and Germans). We can observe significant differences between urban and rural regions, and the majority of white people that choose to live in rural are Afrikaner farmers or industrials. They are descendent of Calvinists, being profoundly conservative and in the Apartheid days, were the soul of the regime as its values were the moral basis of the state rules (assuming themselves as the real and true South Africans, do not recognising black people as South Africans until the 1994 revolution). Regarding black people, the urban ones follow the modern life way of living, highly influenced by American and European urban and sub-urban lives. Rural black groups are very close to old myths, traditions inherited from their ancestors. Black Africans represent 70% of the entire population, white people 11%, coloured about 8% and Indians, Chinese and other minority groups less than 2%. Inside each group there is also significant differences – for example, blacks of Johannesburg are mainly Zulu speakers while Cape Town blacks are more Xhosa, reflecting ancestral and indigenous ties. This diversity among the same group is crucial to understand why there was never a civil war in the country on the 20th problematic century (Independence from English and Dutch and the *Apartheid*).

Technological Analysis

Considering the PESTEL as a research tool, our analysis led us to conclude that Technological Analysis is the most relevant one for nMusic and TRACE due to the nature of the service offered, a music streaming. Based on this, the Technological Analysis of South Africa will be the deeper one and serve as complement to the *Industry Overview,* present on the main text of the work project.

South Africa is currently the most technological country in Africa and seeks to compete with European, USA and Asian Tigers to leverage technologies in terms of investments and business opportunities to attract foreign money, export more and creating a new area of business, able to create jobs, especially for high qualified young workers. According to Euromonitor International, technology improvements in the country are helping other businesses to gain efficiency, lowering production costs and maximizing customer welfare.

We can identify major trends on the technology landscape in South Africa:

- A skyrocket smartphone penetration with the consequently increase in mobile Internet usage and access, driving new digital services (m-commerce);
- As mobile formats rise, fixed-line telephony is decreasing with this consumer shift based on the convenience, faster access and a growing coverage of mobile broadband;
- Increase Internet access, overcoming Television as the leading segment on the Entertainment and Media Market (in 2014, it represented 25% of this market according with PwC);
- Despite spectrum limitations, mobile operators are expanding 4G networks;
- Implementation of the National Broadband Plan to install and/or increase connectivity in rural and small urbanized areas;

Based on Euromonitor, the shift for mobile Internet subscriptions is increasing and in 2/3 years it is expected to overcome fixed-lines telephones. The following figure presents data on this issue from 2008 to 2013 and it is clear the trend written before.

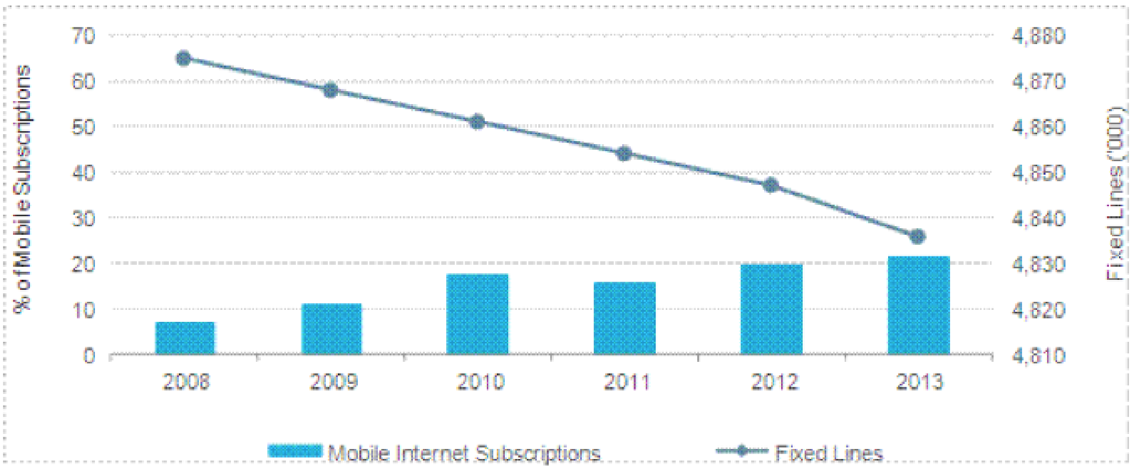


Figure 5 – Comparison between Mobile Internet Subscription and Fixed-Lines Telephony in South Africa on the time frame 2008 – 2013. Source: Euromonitor International

In terms of household consumption in telecom services (Internet access/equipment within), it increased 4.2% on the last year, according with Euromonitor International. An element to consider on technology consumption is that high unemployment rates (see Appendix 3) and high-income inequality are making substantial disparities in penetration along social classes.

In fixed-line market, Telkom SA and Neotel (recently acquired by Vodacom) are the main players, providing 4.8 million fixed active lines in 2013, based on data of the National Broadband Plan. The major supplier of ADSL broadband is Telkom SA, but the company is now shifting to fiber-optics technology as it improves customer experience and Internet speed access. On a country-level, the National Broadband Plan – also called as "South Africa Connect" – has as goal increase broadband coverage: in 2020 the country is expected to have 50% of the population with high speed Internet and in 2030 the goal is to have the entire population with basic speed Internet access. The good and well-developed physical infrastructure alongside with fierce competition among operators is increasing penetration rates on mobile segment. A key fact is also that mobile Internet and smartphones are helping m-commerce to thrive, despite low efforts of the government to promote e-government services. We can also observe that the smartphone penetration has steadily increasing due to the availability of phones at different price points. According to South African Social Media Landscape 2014, the smartphones are impacting growth on social networking (with Facebook achieving 9.4 million users in 2014, an increase of 2.8 million users from the 6.8 million users in the year of 2013) and digital services through apps (music, video, newspapers, etc). The major players on mobile telecom are Vodacom, MTN, Cell C and Telkom Mobile. The following figure presents the Smartphone Market Value on US$ Million on the last years and with projections for the upcoming years.

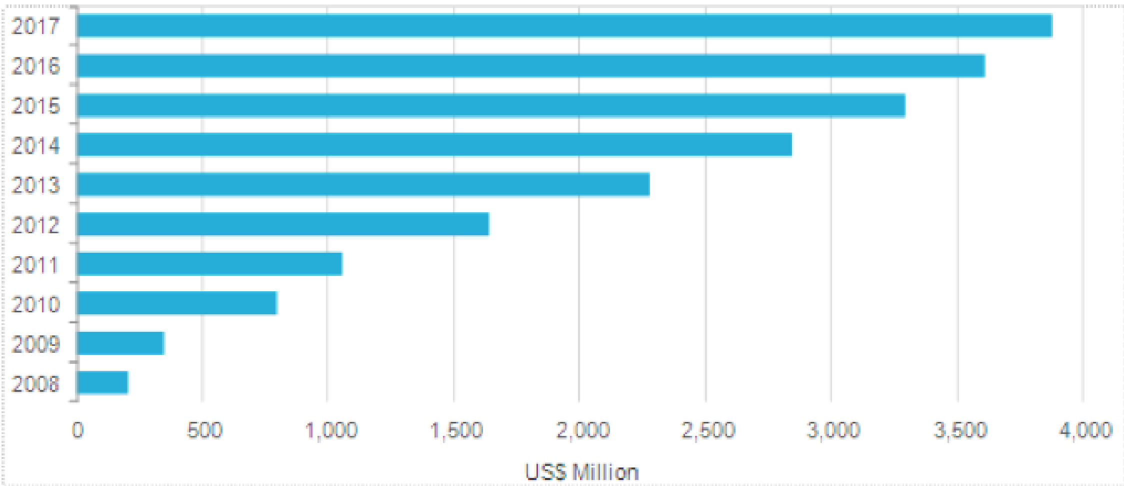


Figure 6 – Smartphones Market Value in South Africa on the time frame 2008 – 2017, US$ Million. Source: Euromonitor International

This technological landscape – specifically regarding telecom sector, e-commerce and m-commerce – will definitely impact nMusic and TRACE partnership and its drivers and challenges must be well understood in order to offer a service that consumers perceived as valuable and useful according with their expectations.

Environmental Analysis

Diamonds, gold, platinum, coal and other metals are the most valuable resources of South Africa. Therefore, the country's authorities have been implementing several plans and actions to maintain long-term sustainability of these assets avoiding damaging actions from major companies that are currently exploring it. Alongside with air quality management, these issues were addressed on the Agenda 21[40] report made by United Nations on collaboration with South African authorities. This report indicates principles, strategies and specific actions to answer to current challenges that the country is face regarding natural resources sustainability - the overall frame is how to connect natural harmony and resources preservation with industrial development, tackling problems of climate change, atmosphere, air pollution or energy. Other acts, such as the National Environment Management: Air Quality Act issued in 2004 or the National Air Quality Management Programme also seeks to provide real actions to

[40] *Agenda 21* Report (Report made by United Nation Division for Economic and Social Affairs on collaboration with Southern African Development Community (SADC), Foreign Affairs, Industry and Trade authorities) http://www.un.org/esa/agenda21/natlinfo/countr/safrica/eco.htm

assure that natural landscape in South Africa is respected. A common trend of all these acts and reports is the emphasis on pedagogical formations and workshop on the community, specially targeting new generations as a way to shape individual and group behaviours.

Legal Analysis

As for any type of business, nMusic and TRACE will have to work under contracts, legal dispositions and contractual agreements, bein obliged to follow the country's rules. The South African legal system is a mix between the Roman-Dutch civil law, British common law with influence of customary law. Nelson Mandela is the "father" of the current Constitution, ratified in 1997.[41] It defines the key principles, the anthem and official languages (problematic issues due to the ethnical diversity and *Apartheid*), the flag and the common legal ground that every government as to endorse and respect, avoiding arbitrary power by executive and legislative bodies, determining their powers and establishing their roles on the country's legal life. Individual rights (free speech, right to work, religious freedom, right to vote and to enter in any part of South Africa, etc.) are guaranteed in the Constitution. Political and jurisdictional rights, obligations and powers are also detailed on this Law, for example, the two parliamentary houses (National Assembly and National Council of Provinces). It also express the checks and balances of the system and determines the level of the President's accountability before the National Assembly. Regarding judicial system there is only one structure: hierarchal and made up by four types of courts, the magistrate, the high courts, the Supreme Court of Justice and the Constitutional judges. Based on the Constitution, the South African President is the commander in chief of the defense forces (although this power is under determined conditions and very well specified, making him accountable to the National Assembly). Police authorities are under national government control, despite this, local and provincial government also presents local policing, but with diminishing power compared to the national police. The criminal law, very strict on a country with high level of crime – especially murders in urban areas – defines how the country deals with crime issues, considering the security, well-being, safety and harmony of all South Africans. The condemnation is based on evidence, penalties can be very hard – although

[41] After the original approval, the Fundamental Law has been changed by 16 amendments.

in 1995 the capital punishment was abolished – like the 1000 years imprisonment time punishment for very special cases, such as serial killers or massive murders.

In terms of contract and business agreements, South Africa follows the Roman-Dutch school of thought. Contracts are understood to be agreements by two or more parties and are enforced by law. They also imply obligation fulfillment and rights and are anchored on legal documentation where the parties involved are obliged to certain duties, assuming the fair and good will of all intervenient. The law of obligations and law of property will be the two main national laws for nMusic/TRACE partnership as they are ultimately connected with proprietary and intellectual rights and contractual term agreements (transfer of ownership, for example), despite the sectorial legal disposition – issued by sector regulators – that also impact the legal framework of the streaming service.

Appendix 5 – Media and Entertainment Market Value

The following figure uses data from 2009, 2013 and 2014 alongside with forecasts to market value of Media and Entertainment. For the nMusic/TRACE service we can identify Music, Internet and Television as the most relevant ones.

							FORECASTS							
	2009	% on Total	2013	% on Total	2014	% on Total	2015	% on Total	2016	% on Total	2017	% on Total	2018	% on Total
Internet	621	11%	1,877	22%	2,418	25%	3,068	29%	3,762	32%	4,449	34%	5,230	37%
Television	1,476	27%	2,243	26%	2,389	25%	2,498	23%	2,630	22%	2,747	21%	2,893	20%
Music	175	3%	153	2%	150	2%	149	1%	150	1%	153	1%	161	1%
Radio	190	3%	299	3%	329	3%	358	3%	387	3%	416	3%	446	3%
Books	299	5%	285	3%	285	3%	285	3%	292	2%	292	2%	292	2%
Films	124	2%	175	2%	190	2%	197	2%	212	2%	226	2%	248	2%
Newspappers	643	12%	796	9%	847	9%	884	8%	935	8%	979	8%	1,030	7%
Video Games	117	2%	175	2%	183	2%	205	2%	226	2%	248	2%	270	2%
Sports	825	15%	1,074	12%	1,205	12%	1,249	12%	1,359	11%	1,432	11%	1,497	11%
Out-of-Home	183	3%	299	3%	321	3%	343	3%	365	3%	380	3%	394	3%
Magazines	438	8%	657	8%	701	7%	745	7%	782	7%	825	6%	869	6%
B2B	424	8%	628	7%	665	7%	701	7%	745	6%	789	6%	833	6%
TOTAL	5,515		8,663		9,682		10,682		11,845		12,936		14,164	

Figure 7 – Media and Entertainment Market Value (Million Euro, 2009, 2013 – 2018 time frame).

Source: PwC

Appendix 6 – Comparison between Physical and Digital Music Unit Sales

The unit sales of Physical and Digital Music help us to understand the structural shift occurring in the Music Industry. The trend is clear and CAGR of both types of music evidently shows that as physical recorded music declines, digital surges and takes the lead of music unit sales after 2015.

							FORECASTS				
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	CAGR (2013 - 2018)
Physical	20	19	17	17	15	13	12	11	10	9	-9.7%
Digital	1	1	1	1	8	11	14	16	17	18	17.6%
TOTAL UNIT SALES	21	20	18	18	23	24	26	27	27	27	3.3%

Figure 8 – Comparison between Physical and Digital Music Unit Sales (Million, 2009 – 2018 time frame). Source: PwC

Appendix 7 – TRACE Satellite Footprint

TRACE, as network of TV channels present in 60 countries has a satellite coverage that includes almost the entire world. For nMusic this can be a positive sign, as TRACE can start expand streaming services to other countries. Following its worldwide satellite footprint is presented:

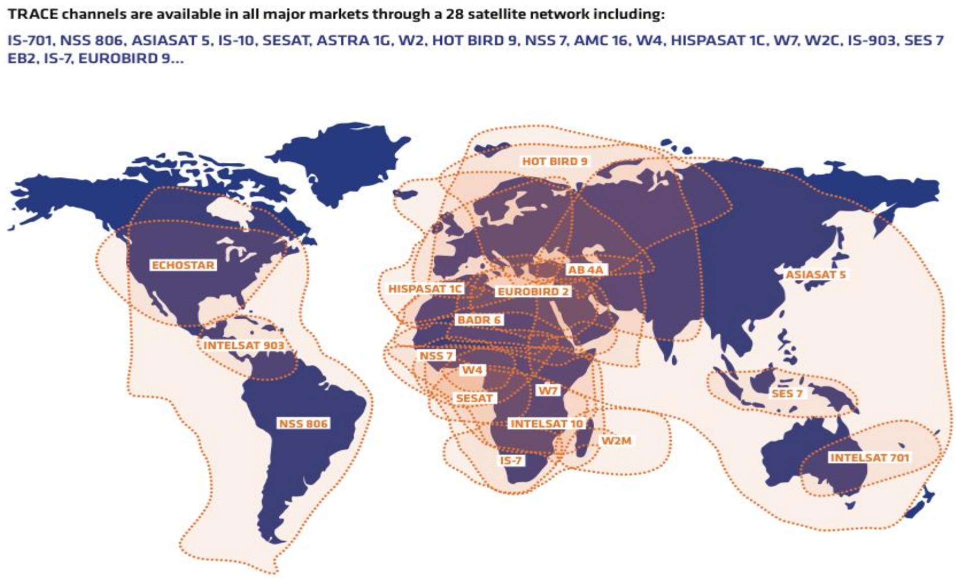


Figure 9 – TRACE Worldwide Satellite Footprint. Source: TRACE Corporate Manifesto

Appendix 8 – B2B2C Business Model

nMusic uses a B2B2C business model operating as a private label that seeks partnerships with recognized brands from diverse sectors to develop, under their name and brand, a streaming service. The B2B2C is typically an e-commerce business model andcombines the Business to Business (B2B) side, performed by nMusic while developing its platform and dealing with music licenses and the Business to Consumer (B2C) side, TRACE responsibility of engaging audience, attract and retain customers, as a consumer-oriented company. In theory, this arrangement provides mutual benefits, as each company focus their efforts on the business aspect where has developed its expertise and resources. The following figure presents a scheme of how this business model works:

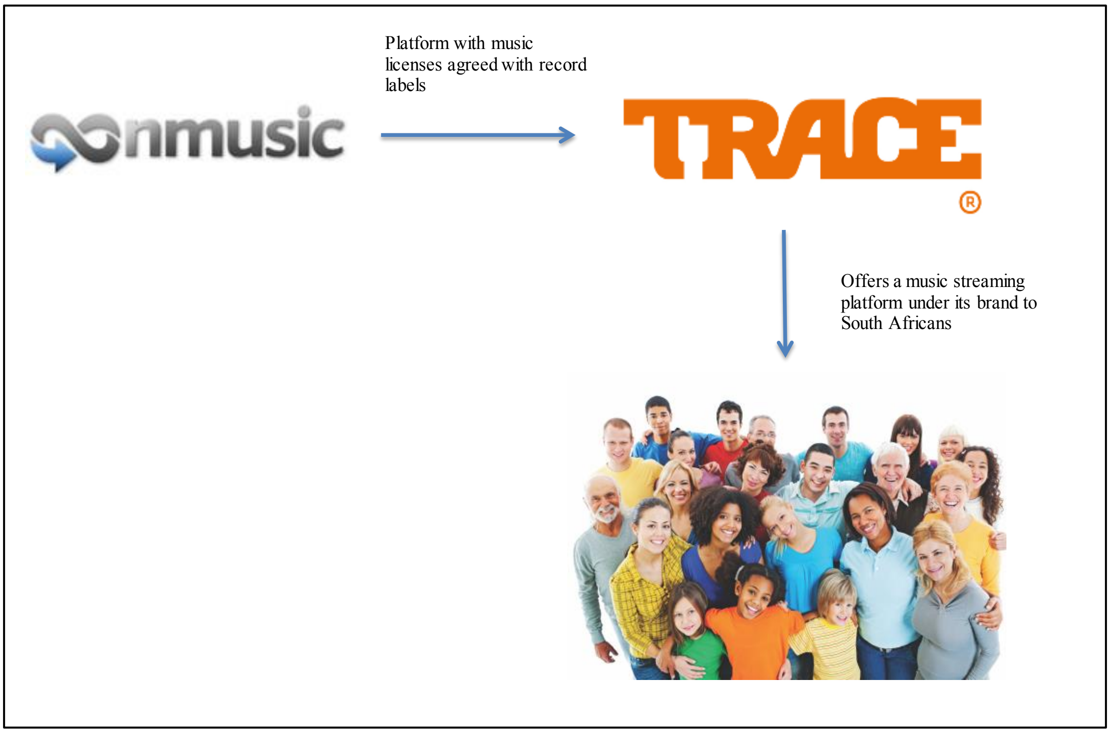


Figure 10 – Scheme of B2B2C on the nMusic/TRACE partnership.

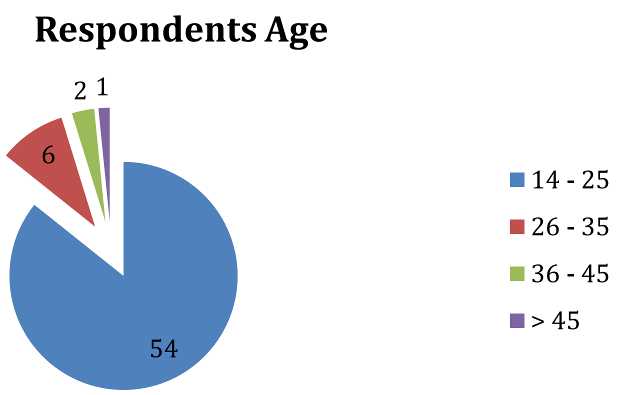
Appendix 9 – Market Survey

In order to have a more knowledge of South African market, a market survey was conducted to assess the awareness of TRACE, the attitude before TRACE offering a streaming service, the willingness to pay a subscription, which features are most valued and the price ranges that consumers perceived as fair according to the service offering.

Our online survey conducted during the months of October and November 2014 collected 63 valid answers by residents in South Africa. Following we present the structure of the survey alongside with the results obtained for each question:

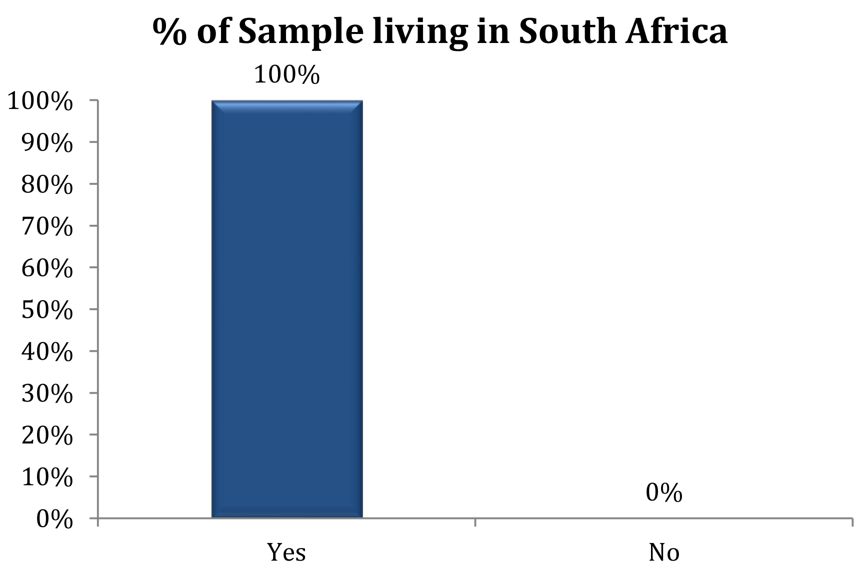
1 - What is your age?

14 – 25	54
26 – 35	6
36 – 45	2
> 45	1



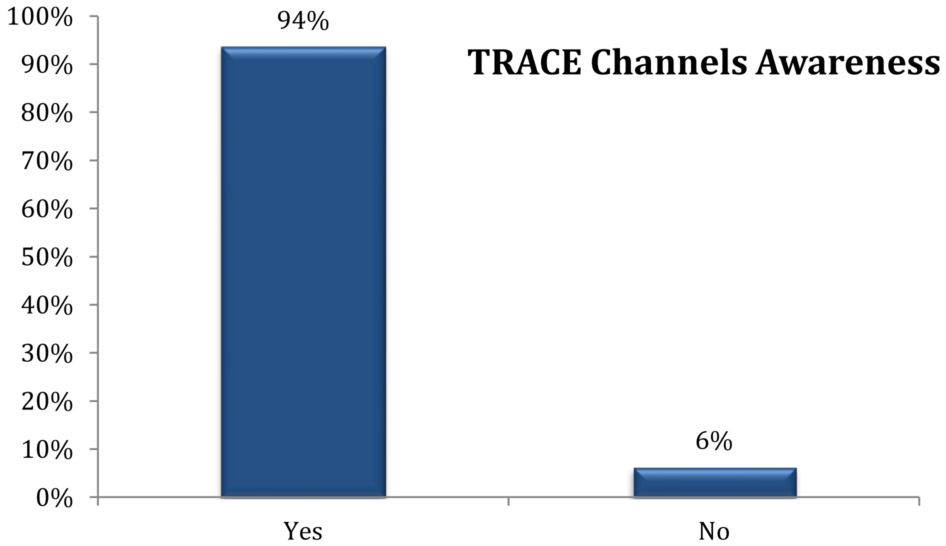
2 - Do you currently live in South Africa?

Yes	63	(100%)
No	0	(0%)



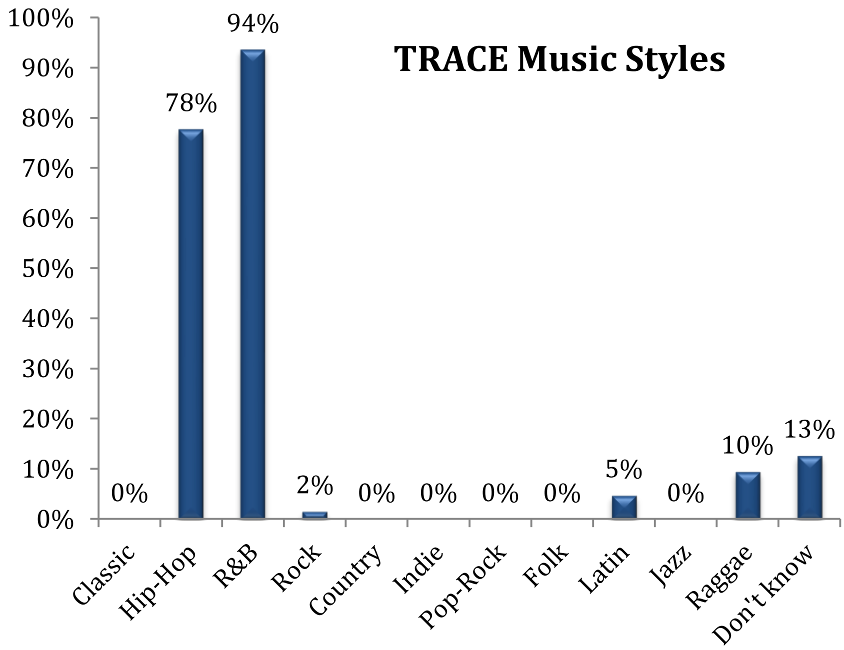
3 - Are you aware of TRACE Tv channels?

Yes	59	(94%)
No	4	(6%)



4. If someone asks you to match TRACE content with music styles, which ones would you choose? (Please indicate 2)

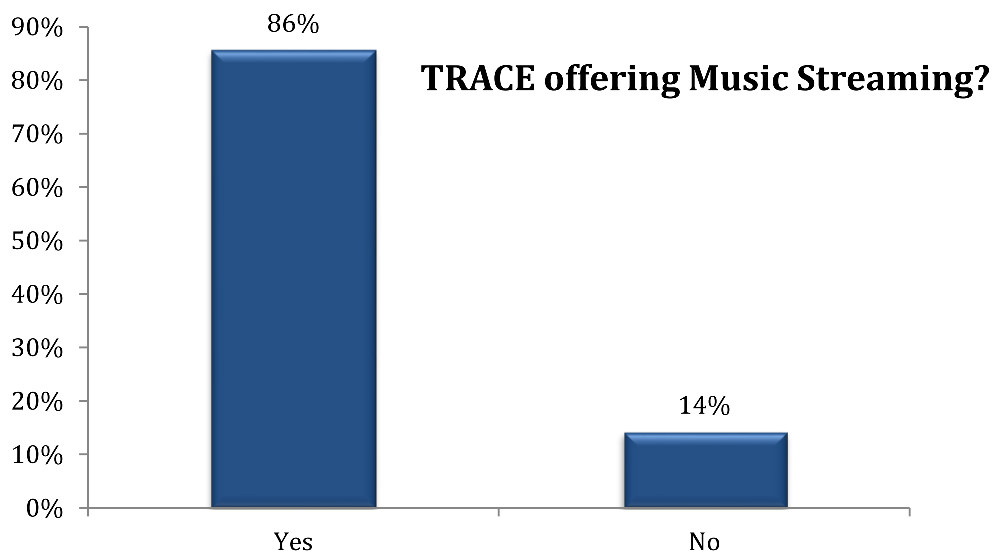
Classic	0 (0%)
Hip-Hop	49 (78%)
R&B	59 (94%)
Rock	1 (2%)
Country	0 (0%)
Indie	0 (0%)
Pop Rock	0 (0%)
Folk	0 (0%)
Latin	3 (5%)
Jazz	0 (0%)
Reggae	6 (10%)
Don't know	8 (13%)



5 - Do you think that offering a streaming service would fit with TRACE music channels?

Yes 54 (86%)

No 9 (14%)

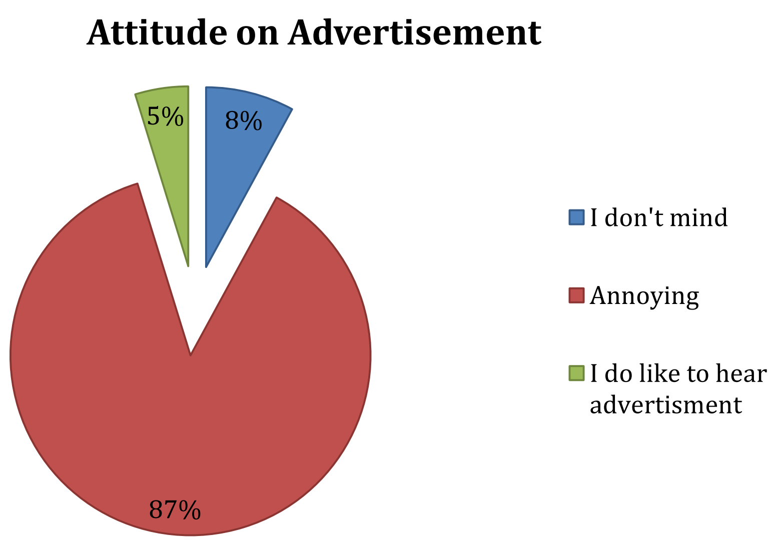


6 - Can you describe your feelings about audio advertisement on music streaming platforms?

I don't mind 5 (8%)

Annoying 55 (87%)

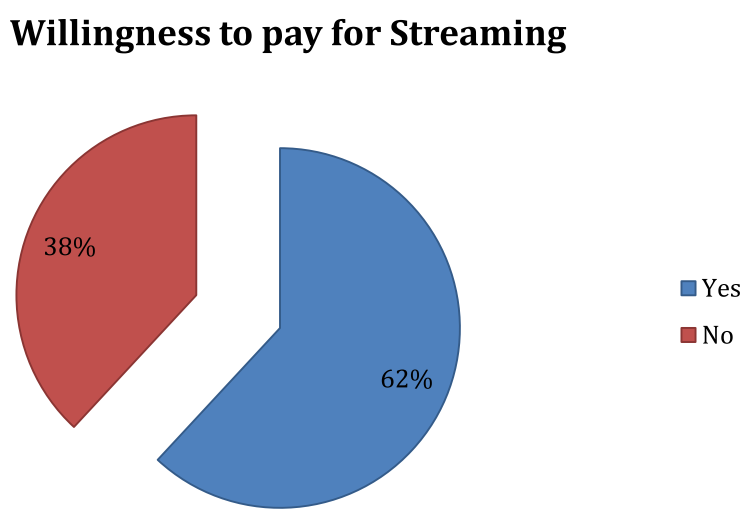
I do like to hear advertisement 3 (5%)



7. Are you willing to pay a monthly fee for a streaming service?

Yes 39 (62%)

No 24 (38%)



8. Which features from the list below would increase your willingness to pay for a streaming service? (You can choose as many as you want)

Downloads 58 (92%)

Offline mode 39 (62%)

Recommendations 24 (38%)

Video clips 49 (78%)

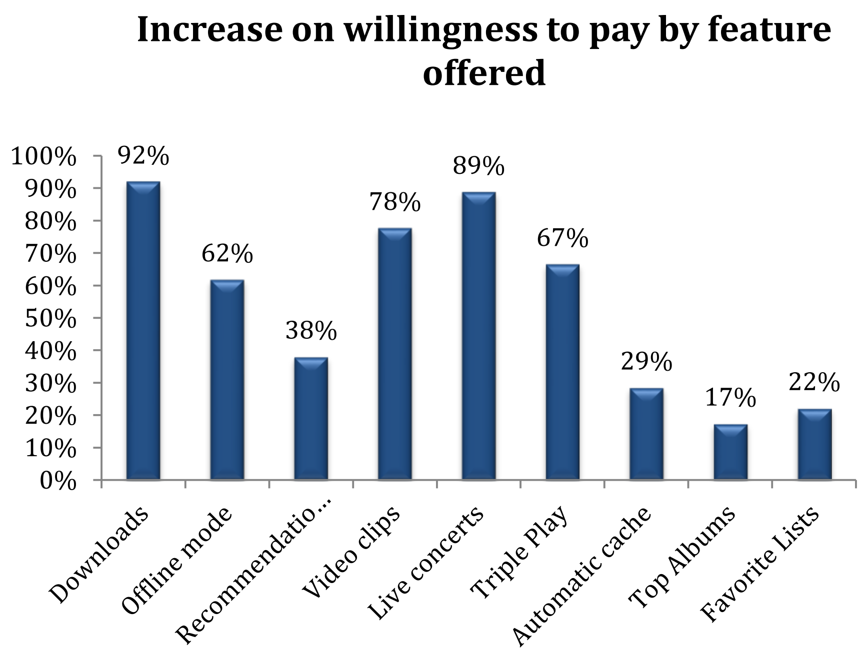
Live concerts 56 (89%)

Triple Play 42 (67%)

Automatic cache 18 (29%)

Top Albums 11 (17%)

Favourite Lists 14 (22%)



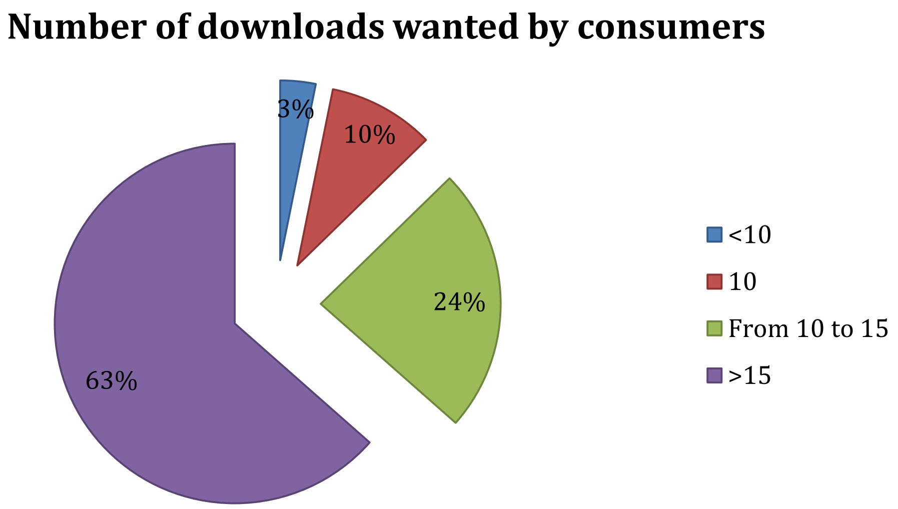
9. If downloads are included on this service, how many (per month) do you think would be a good number?

<10 2 (3%)

10 6 (10%)

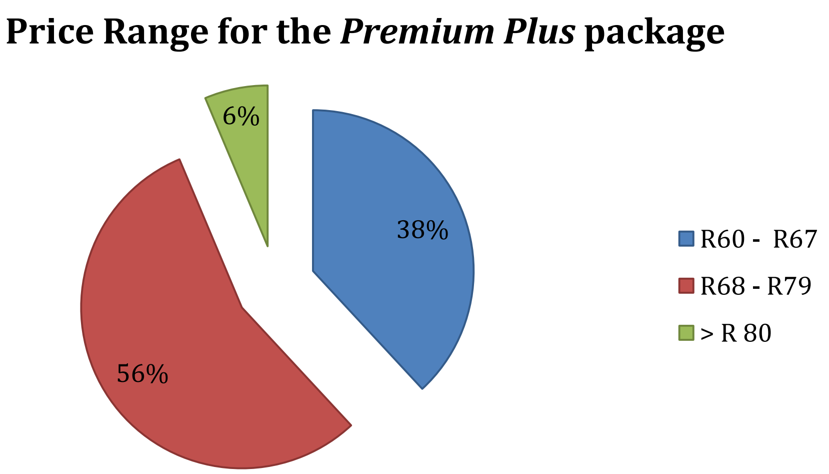
From 10 to 15 15 (24%)

>15 40 (63%)



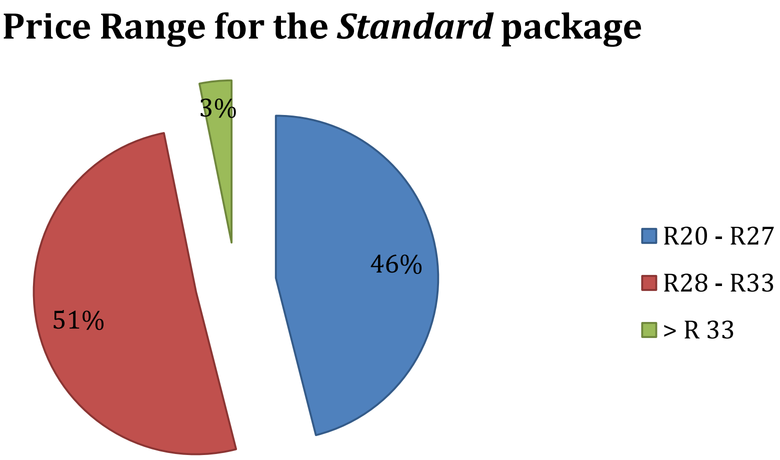
10. For a multi platform (TV, computer, smartphone and tablet) access with offline mode available, video-clips and monthly downloads, which price range do you think it is suitable?

R60 (4.30€) - R67 (4.80€)	24 (38%)
R68 (4.86€) - R79 (5.64€)	35 (56%)
> R 80 (5.72€)	4 (6%)



11. Consider the opposite scenario, a steaming service only available on destkop offering offline mode but with no monthly downloads, which price range do you think it is suitable?

R20 (1.40€) - R27 (1.93€)	29 (46%)
R28 (2.00€) - R33 (2.36€)	32 (51%)
> R 33 (2.36€)	2 (3%)



Appendix 10 – nMusic Industry Mapping

Following it is presented the graphical representation of nMusic Industry Mapping for its venture in South Africa:

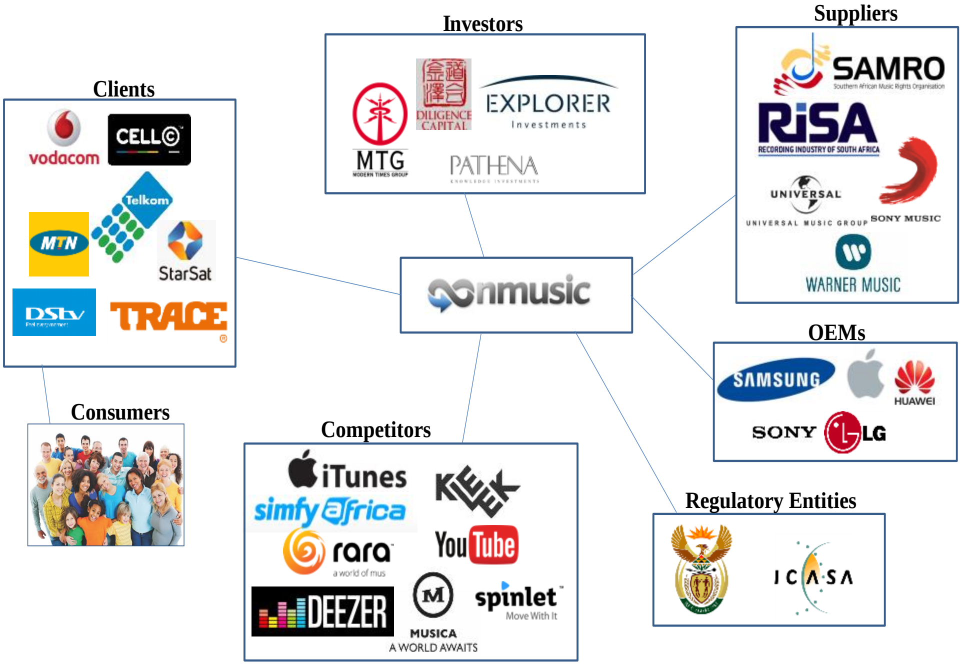


Figure 11 – nMusic Industry Mapping in South Africa

Appendix 11 – Streaming Competitors Comparison

Following it is presented a general comparison between major streaming companies operating in South Africa, adding the proposed P&S offering of nMusic/TRACE and its correspondent price scheme. We must add that our proposal regarding price scheme is different from the usual 2-tier service that competitors present. As a consequence, on the "Highest Price" column, for nMusic/TRACE is presented 2 prices:

- A Premium Package for 4.50 that matches Rara, Deezer, Simfy and Rdio in terms of features offering (triple-play and video-clips are the Point of Difference);
- The Premium Plus Package sold by 5.50€ as no parity with other premium packages offered by competitors, as it offers 20 downloads per month, beyond triple-play, video-clips, offline mode and sharing tools.

The next figure presents the comparison made:

	Downloads	Offline	Free Mode	Ad-free	Sharing (Fb, Twitter)	Triple Play	Video-clips	Partner	Chepeast Package	Highest Package
Rara	✗	✓	✗	✓	✓	✗	✗	-	2.50 €	5.05 €
Deezer	✗	✓	✓	✓	✓	✗	✗	Vodacom	2.20 €	4.40 €
The Kleek	✗	✓	✗	✓	✓	✗	✗	Universal, Samsung	N/A	N/A
Simfy	✗	✓	✗	✓	✓	✗	✗	MTN	1.80 €	4.40 €
Rdio	✗	✓	✗	✓	✓	✗	✗	-	1.80 €	4.40 €
nMusic	✓	✓	✗	✓	✓	✓	✓	TRACE	2.20 €	4.50€ / 5.50€

Figure 12 – Comparison between major Streaming companies in South Africa and nMusic/TRACE offering.

Appendix 12 – nMusic P&L Statement (Key Items)

On the next figure it is presented the key items on nMusic's Profit and Losses Statement on the years of 2012 and 2013.

	2013	% of Revenue	2012	% of Revenue
Revenues	3,032,431 €		2,103,448 €	
Music Licenses	2,033,680 €	67.1%	1,730,282 €	82.3%
Wages	415,182 €	13.7%	263,843 €	12.5%
EBITDA	740,407 €	24.4%	132,393 €	6.3%
EBT	573,425 €		21,138 €	
Taxes	69,154 €		20,843 €	
Net Profit	504,271 €	16.6%	295 €	0.01%

Figure 13 – nMusic P&L. Source: Dun and Bradstreet Informa

As we can see, Music Licenses (paid mainly to record labels) represented on average 75% of nMusic revenues on the last years. According to nMusic executives, on 2014 – financial data non available yet – they are lowering this cost. This is the basis of our assumption of 70% of revenues paid to record labels made on the chapter *A Profitable Partnership: Revenue and Cost Structure* to estimate costs and potential profits in the South African venture.

Appendix 13 – Potential Scenarios

To assess potential gains that nMusic can have with this movement to South Africa, a scenarios-analysis was conducted to present a clear and measurable idea of how much it can profit (and which are the main costs). According with our Price Scheme (see figure below), the nMusic/TRACE will receive revenues from its 3 package (the Standard, the Premium and the Premium Plus).

Package	Price Range	Main Features	Reasoning
Standard	EUR 2.20 / Month	Desktop App only, with offline mode but no downloads and no videoclips	Targeting low cost users on similar price to the one offered by Rdio, Simfy and Deezer, but with one extra feature compared to them: the offline mode. **Market Survey: 51% of respondents stated that this price is adequate for the package offering.**
Premium	EUR 4.50 / Month	Muti Devices access, all features included	Tageting premium offers from competitors, with several extras: TV access, video-clips and downloads. Granting the possibility of downloads is a way to compete with the successful iTunes.
Premium Plus	EUR 5.50 / Month	Muti Devices access, all features with 20 downloads	This offer goes beyond competitors best packages by offering all the features and the possibility of downloading 50 songs per month (same point regarding iTunes). **Market Survey: 56% of respondents stated that this price is adequate for the package offering.**

Figure 14- Price Scheme of nMusic/TRACE Streaming service

The service will have the following Cost Structure, allowing the net profits to be divided on a 50/50 basis between nMusic and TRACE:

Standard	Premium	Premium Plus	
2.20 €	**4.50 €**	**5.50 €**	Revenue per user
0.31 €	0.63 €	0.77 €	VAT on Digital Goods (14%)
1.89 €	**3.87 €**	**4.73 €**	
0.24 €	0.48 €	0.59 €	Fee to SAMRO (12.5%)
1.66 €	**3.39 €**	**4.14 €**	
1.16 €	2.37 €	2.90 €	Fee to Record Labels (70%)
0.50 €	**1.02 €**	**1.24 €**	
0.03 €	0.06 €	0.07 €	Bandwith cost (6%)
0.47 €	0.95 €	1.17 €	Net Profit per User
0.23 €	**0.48 €**	**0.58 €**	nMusic Net Profit per User

Figure 15- nMusic/TRACE Cost Structure

Our analysis undertook 3 scenarios - the Best, the Most Likely and the Worst case. The big difference among them is how users allocate themselves by package, reflecting the capacity of moving customers towards more Premium packages. We also assume that after 6 months there will be 100 000 users and after 12, 200 000 users (10% of TRACE customer base on its TV channels):

- ***BEST CASE SCENARIO***

On the Best case, we assume that Premium Plus will be the most chosen one, providing this scenario in terms of net profit (*in the end of 1st year the net profit for nMusic will be 108,531.40€ monthly):*

Month	TOTAL USERS	STANDARD USERS	% ON TOTAL	PREMIUM USERS	% ON TOTAL	PREMIUM PLUS USERS	% ON TOTAL	Monthly Net Profit for nMusic
1	16600	3320	20%	6640	40%	6640	40%	7,820.18 €
2	33200	4980	15%	13280	40%	14940	45%	16,221.59 €
3	49800	4980	10%	22410	45%	22410	45%	24,940.03 €
4	66400	9960	15%	23240	35%	33200	50%	32,795.43 €
5	83000	8300	10%	29050	35%	45650	55%	42,447.37 €
6	99600	9960	10%	29880	30%	59760	60%	**51,465.23 €**
7	116200	11620	10%	40670	35%	63910	55%	59,426.31 €
8	132800	13280	10%	46480	35%	73040	55%	67,915.79 €
9	149400	14940	10%	44820	30%	89640	60%	77,197.84 €
10	166000	8300	5%	49800	30%	107900	65%	88,681.53 €
11	182600	9130	5%	45650	25%	127820	70%	98,518.40 €
12	199200	9960	5%	39840	20%	149400	75%	**108,531.40 €**

Figure 16 – Monthly Net Profit for nMusic on the Best Case Scenario

This scenario will reflect in terms of profits the following distribution of users per package:

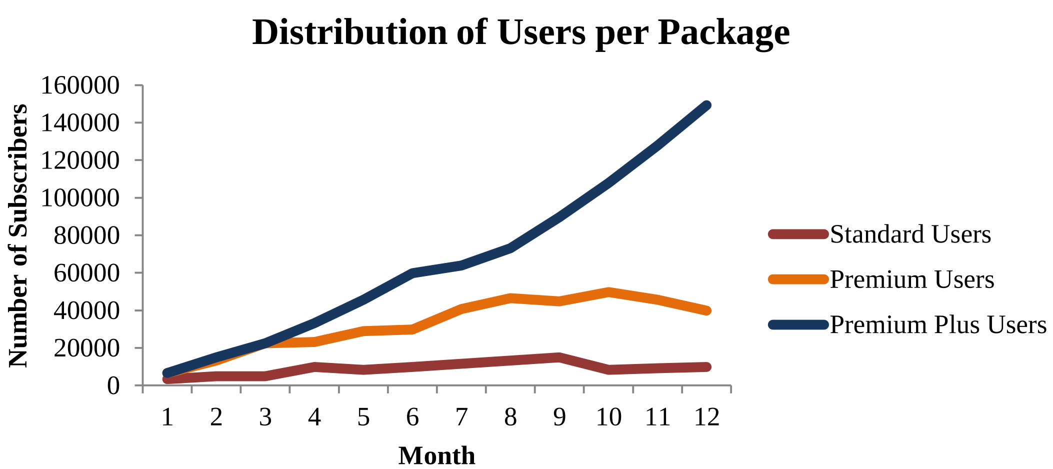


Figure 17 –Distribution of Users per package on the Best Case Scenario

- ***WORST CASE SCENARIO***

On the Worst case, the service fails to sell its premium offering – either Premium or Premium and consumers stay mainly on the Standard subscription, leading to smaller revenues and therefore fewer profits (*in the end of 1st year the net profit for nMusic will be 62,138.72€ monthly):*

Month	TOTAL USERS	STANDARD USERS	% ON TOTAL	PREMIUM USERS	% ON TOTAL	PREMIUM PLUS USERS	% ON TOTAL	Monthly Net Profit for nMusic
1	16600	6640	40%	8300	50%	1660	10%	6,481.59 €
2	33200	14940	45%	14940	45%	3320	10%	12,558.08 €
3	49800	22410	45%	22410	45%	4980	10%	18,837.12 €
4	66400	29880	45%	26560	40%	9960	15%	25,468.42 €
5	83000	41500	50%	29050	35%	12450	15%	30,822.78 €
6	99600	49800	50%	34860	35%	14940	15%	**36,987.33 €**
7	116200	63910	55%	40670	35%	11620	10%	41,117.58 €
8	132800	73040	55%	46480	35%	13280	10%	46,991.52 €
9	149400	89640	60%	44820	30%	14940	10%	51,042.52 €
10	166000	99600	60%	58100	35%	8300	5%	55,833.26 €
11	182600	118690	65%	54780	30%	9130	5%	59,188.54 €
12	199200	139440	70%	49800	25%	9960	5%	**62,138.72 €**

Figure 18 – Monthly Net Profit for nMusic on the Worst Case Scenario

This scenario will reflect in terms of profits the following distribution of users per package:

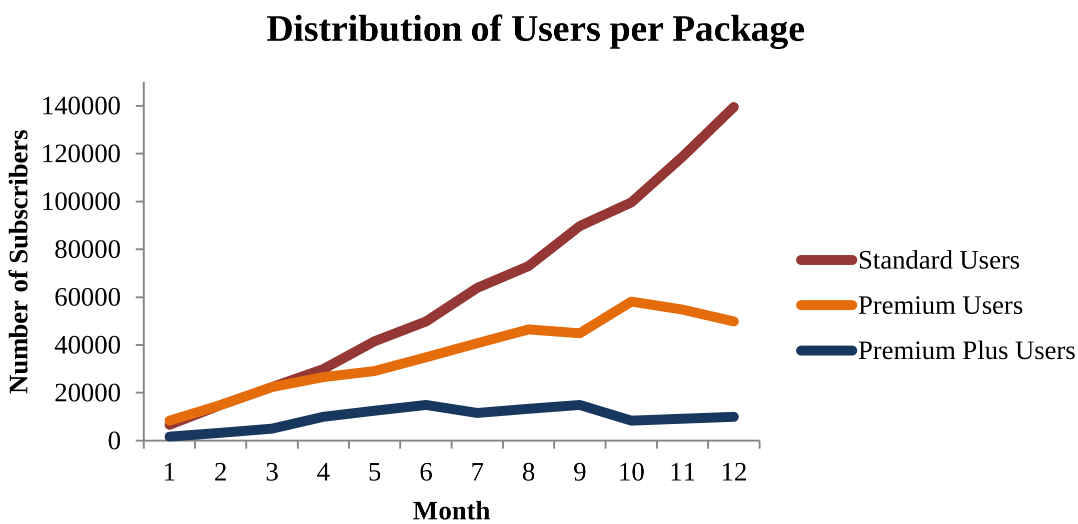


Figure 19 –Distribution of Users per package on the Worst Case Scenario

- ***MOST LIKELY SCENARIO***

The Most Likely Scenario assumes a structure similar to Normal Distribution with the majority falling on Premium and two smaller groups, one the left (Standard) and one the right (Premium Plus). *In the end of 1st year the net profit for nMusic will be 91,728.58€ monthly:*

Month	TOTAL USERS	STANDARD USERS	% ON TOTAL	PREMIUM USERS	% ON TOTAL	PREMIUM PLUS USERS	% ON TOTAL	Monthly Net Profit for nMusic
1	16600	2490	15%	11620	70%	2490	15%	7,582.40 €
2	33200	4980	15%	21580	65%	6640	20%	15,340.94 €
3	49800	7470	15%	29880	60%	12450	25%	23,275.60 €
4	66400	9960	15%	36520	55%	19920	30%	31,386.39 €
5	83000	12450	15%	41500	50%	29050	35%	39,673.32 €
6	99600	14940	15%	49800	50%	34860	35%	**47,607.98 €**
7	116200	23240	20%	58100	50%	34860	30%	53,508.34 €
8	132800	26560	20%	66400	50%	39840	30%	61,152.39 €
9	149400	29880	20%	74700	50%	44820	30%	68,796.44 €
10	166000	33200	20%	74700	45%	58100	35%	77,321.14 €
11	182600	36520	20%	91300	50%	54780	30%	84,084.53 €
12	199200	39840	20%	99600	50%	59760	30%	**91,728.58 €**

Figure 20 – Monthly Net Profit for nMusic on the Most Likely Scenario

This scenario will reflect in terms of profits the following distribution of users per package:

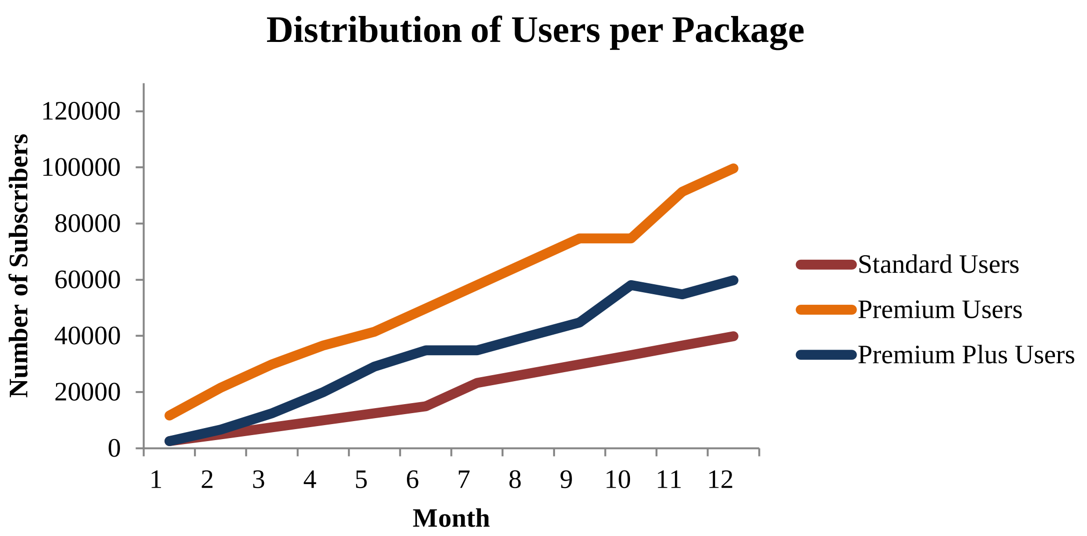


Figure 21 –Distribution of Users per package on the Most Likely Scenario